S. HRG. 98-298

OVERSIGHT OF FEDERAL DEBT COLLECTION

HEARING

BEFORE THE

SUBCOMMITTEE ON ENERGY, NUCLEAR PROLIFERATION, AND GOVERNMENT PROCESSES

OF THE

COMMITTEE ON GOVERNMENTAL AFFAIRS UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

FIRST SESSION

MAY 25, 1983

Printed for the use of the Committee on Governmental Affairs

U.S. GOVERNMENT PRINTING OFFICE
23-137 O WASHINGTON: 1983

5401-70

COMMITTEE ON GOVERNMENTAL AFFAIRS

WILLIAM V. ROTH, JR., Delaware, *Chairman*

CHARLES H. PERCY, Illinois
TED STEVENS, Alaska
CHARLES McC. MATHIAS, JR., Maryland
WILLIAM S. COHEN, Maine
DAVID DURENBERGER, Minnesota
WARREN B. RUDMAN, New Hampshire
JOHN C. DANFORTH, Missouri
THAD COCHRAN, Mississippi
WILLIAM L. ARMSTRONG, Colorado

THOMAS F. EAGLETON, Missouri
HENRY M. JACKSON, Washington
LAWTON CHILES, Florida
SAM NUNN, Georgia
JOHN GLENN, Ohio
JIM SASSER, Tennessee
CARL LEVIN, Michigan
JEFF BINGAMAN, New Mexico

JOAN M. MCENTEE, *Staff Director and Chief Counsel*
IRA S. SHAPIRO, *Minority Staff Director and Chief Counsel*

SUBCOMMITTEE ON ENERGY, NUCLEAR PROLIFERATION, AND GOVERNMENT PROCESSES

CHARLES H. PERCY, Illinois, *Chairman*

DAVID DURENBERGER, Minnesota
WILLIAM S. COHEN, Maine
JOHN C. DANFORTH, Missouri

JOHN GLENN, Ohio
HENRY M. JACKSON, Washington
CARL LEVIN, Michigan

WILLIAM A. STRAUSS, *Chief Counsel and Staff Director*
ALAN MERTZ, *Professional Staff Member*
ELAINA NEWPORT, *Staff Assistant*
LEONARD WEISS, *Minority Staff Director*
KATHRYN H. FROELICH, *Chief Clerk*

CONTENTS

Opening statements: Page

Senator Percy 1
Senator D'Amato 3

WITNESSES

WEDNESDAY, MAY 25, 1983

Harold I. Steinberg, Associate Director for Management, Office of Management and Budget, accompanied by Jack Donahue, Director, Debt Collection Project, OMB 6

Roger Feldman, Comptroller, Department of State, accompanied by Ann Swift, Acting Director, Citizens Emergency Center, Department of State, and Charles F. Koeneman, Chief of the General Accounting Division, Department of State 26

John H. Kelso, Deputy Administrator, Health Resources and Services Administration, Department of Health and Human Services, accompanied by Thomas D. Hatch, Director, Bureau of Health Professionals 30

Robert B. Webber, General Counsel, Small Business Administration, accompanied by Earl Chambers, debt collection official, Small Business Administration 35

Ralph Olmo, Comptroller, Department of Education; Richard Hastings, Director, Student Financial Assistance, Department of Education; Jack Reynolds, coordinator, collection task force, Department of Education; J. Paul McGrath, Assistant Attorney General, Civil Division, Department of Justice; and Bob Ford, Deputy Assistant, Department of Justice 54

Bernard D. Landau, attorney, Hayt, Hayt & Landau, New York, N.Y.; Alan D. Reffkin and Robert S. LeWinter, partners of Bernard D. Laudau; G. L. Dawson, assistant vice president, GC Services Corp., Houston, Tex., accompanied by Ed Burke, corporate counsel, and Carolyn Webber, Washington representative 92

ALPHABETICAL LIST OF WITNESSES

Burke, Ed: Testimony 92

Chambers, Earl: Testimony 35

Dawson, G. L.:
- Testimony 92
- Prepared statement 118

Donahue, Jack: Testimony 6

Feldman, Roger: Testimony 26

Ford, Bob: Testimony 54

Hastings, Richard: Testimony 54

Hatch, Thomas D.: Testimony 30

Kelso, John H.: Testimony 30

Koeneman, Charles F.: Testimony 26

Landau, Bernard D.:
- Testimony 92
- Prepared statement 101

LeWinter, Robert S.: Testimony 92

McGrath, J. Paul.:
- Testimony 54
- Prepared statement 83

Olmo, Ralph:
- Testimony 54
- Percentage of Collection Dollars, by source, fiscal year 1979 through fiscal year 1983 (chart) 56
- Prepared statement 78

	Page
Reffkin, Alan D.: Testimony	92
Reynolds, Jack: Testimony	54
Steinberg, Harold I.:	
Testimony	6
Organization chart	9
Prepared statement	16
Swift, Ann: Testimony	26
Webber, Carolyn: Testimony	92
Webber, Robert B.:	
Testimony	35
Letter to Senator Percy, Aug. 5, 1983	39
Prepared statement	46

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

Criminal Fine Collections (chart)	69
Statement of H. Grant Lappin, Jr., president of Accounts Management Corp.	127
Letter to Senator Percy from Paul F. Leary, associate director, financial operations, Harvard University, May 23, 1983	133

OVERSIGHT OF FEDERAL DEBT COLLECTION

WEDNESDAY, MAY 25, 1983

U.S. SENATE,
SUBCOMMITTEE ON ENERGY,
NUCLEAR PROLIFERATION, AND GOVERNMENT PROCESSES,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, D.C.

The subcommittee met at 10 a.m., in room SD–138, Dirksen Senate Office Building, Hon. Charles H. Percy (chairman of the subcommittee) presiding.

Present: Senator Percy.

Also Present: Senator D'Amato.

OPENING STATEMENT OF SENATOR PERCY

Senator PERCY. I would like to welcome everyone to this hearing on what I consider to be one of the most cost-effective management initiatives that I have been involved in in 17 years in the Senate. I would like to welcome Senator D'Amato, who has been so extraordinarily cooperative and helpful, though not a member of this committee.

He has taken a deep interest in the area of debt collection, and has facilitated and helped this committee find more cost-effective ways of going about our job.

It was just 1½ years ago that I chaired a hearing in which I had the unpleasant task of calling to task one of our Nation's most prestigious schools, Harvard University.

I asked Harvard to explain why 23 percent of its medical school graduates—many of whom were on Harvard's faculty and earning big salaries as physicians—who had received student loans, were delinquent in repaying these loans.

In fact, I called the president of Harvard at one point just to impress upon him the importance that I attached to these hearings and how I felt the reputation of the great institution was at stake.

Since that hearing, due to what Harvard describes as an all-out effort, its delinquency rate has dropped to about 5 percent. That is about an 80-percent reduction, a tremendous, dramatic improvement. As a former industrialist and businessman, it seemed to me that if I ran a business the way we were running the business of the Government, we would be utterly bankrupt.

We are, it seems, sometimes, but certainly it shouldn't be because of the inability or the unwillingness of the Federal Government to find ways to get people and cause people to pay their debts to the Federal Government.

I have just left a group of about 80 Illinois farmers and a discussion of the credit program for farmers. I received the impression that farmers are going to pay their bills. The ultimate threat of foreclosure must remain for those who do not pay their bills. We cannot let these people off the hook. What we were doing with many of the Federal loans that were outstanding was simply not following up on them.

We weren't tenacious, we were not running ourselves as a business, we were running ourselves as a bureaucracy and it simply had a record that any business would consider a disgrace. And it was a disgrace.

I want to say to Harvard University and other universities that have shown progress how really proud we are of the fact that since our hearing 1½ years ago they have had a complete change of course and attitude.

I think they have done an outstanding job.

At another hearing last year, I expressed concern to the Department of Education about the 50,000-plus current and former Federal employees who were delinquent in their student loans.

Can you imagine anything more incongruous than Federal workers who have received their degrees with help from the same government that employs them—some of them earning as much as $50,000—not paying back their student loans?

The Department, then, mailed letters to these borrowers and promptly received $2.3 million in repayment. It also spent $6,000 to send mailgrams to delinquent debtors who had borrowed under the Cuban loan program, receiving about $300,000 in repayment. That is not a bad return on a $6,000 investment.

Again, I want to commend the Department of Education and, in particular, Secretary Bell. I participated with him in a ceremony at the Department when they began processing the notifications to Federal employees, and it is a program that has paid off.

These cases are not isolated success stories—they show that these loans can be collected if we put our minds to it. It is that simple.

In fiscal year 1982, our tough new debt collection procedures reaped over $2 billion in revenues that otherwise would have been lost to taxpayers. In 1983, the figure will be close to $3 billion.

This debt collection program is the most successful management improvement initiative I have seen in my 17 years in the Senate. The Reagan administration is to be commended for a job well done, and for the enthusiasm with which David Stockman and his colleagues at OMB and in the White House have approached the program and the personal leadership the President has given to it. They really have done an outstanding job.

It might be tempting for us to declare victory over our debt collection problems and then move on to other problems.

Believe me, this would be a mistake. We still have a long way to go. The Federal Government is still owed a staggering $40 billion in delinquent debts—almost $400 for every taxpayer in this country.

The Federal Government needs to fight hard to collect these taxpayer dollars. If it means going to court to collect, we will. It is time for delinquent borrowers to get the message that their Government, the taxpayers and the administration are very serious about this matter.

The Debt Collection Act of 1982, which was signed into law last

October, gives the Federal Government several useful tools, including the authority for Federal agencies to contract with private collectors. But many of the loans now with collection agencies—especially the hundreds of thousands of student loans—will eventually need to be taken to court.

Right now many of the 26,000 student loan cases, which should be taken to court, are languishing at the Justice Department, which is just not equipped to handle this volume.

For this reason Senator D'Amato and I have introduced legislation which will allow the Federal Government to contract loan litigation with private attorneys. This will put some real teeth into Federal debt collection. I am very pleased to have Senator D'Amato with me this morning.

The word is out to defaulters across the Nation that Uncle Sam is serious about debt collection. Take the case of a prominent doctor who, years behind on his student loan, had his accountant send a letter explaining why, despite an after tax monthly income of $8,000, he was unable to pay $90 per month. His auto cost him nearly $1,000 per month. His debts to banks and other creditors cost about $2,000 per month. After deducting several thousand dollars for living expenses and other necessaries, he had, he said, only $25 left for his medical school loan. But the medical school he attended was not convinced of his hardship.

It got fed up with him. It made him pay up. And he paid up.

Some debtors do face real hardships, making repayment difficult, and we have to be sensitive to that, and want to be. But the plain fact is that most borrowers are perfectly able to repay. By collecting, we bolster the Federal loan funds for the benefit of future generations of borrowers. Having increased collections by $156 million last year, for example, the Small Business Administration can now make more money available for future loans. The same is true for student loans.

That is why I am holding this hearing this morning, and that is why I will continue to hold hearings until I am sure that every collectible cent is being returned to the American taxpayer for the benefit of future generations of Americans, and to restore the integrity of the U.S. Government.

This is a question of integrity. I think the most tragic part of it all is that the word got through from colleges and universities across the country that these aren't loans, that you just change your address, send the stuff back, and the computer pulls you out after three letters and you never hear from them again. If they think our Government is that inefficient, and it was, I believe they have got another thing coming now.

Senator D'Amato.

OPENING STATEMENT OF SENATOR D'AMATO

Senator D'AMATO. Mr. Chairman, let me thank you and the committee for affording me the opportunity to participate in today's hearing. I also commend you for your outstanding leadership, not only today but in the past, and for your persistence to see to it that our Nation's debts are legitimately and properly collected. In fiscal year

1982 there was more than $33 billion of outstanding debt. This was an increase of some 37 percent in 2 years. A shocking $13 billion alone was in nontax delinquencies. So, Mr. Chairman, the work that you and the committee have undertaken is truly important.

You have made tremendous progress in beginning to focus national attention and congressional attention on these outstanding delinquencies. We are not talking, as you so aptly put it, about the case of the widow who has a delinquent tax bill. We are talking about the kinds of situation where business people, entrepreneurs, lawyers, and doctors, in many cases, made deliberate and calculated business decisions that they need not pay back their loans to the Government and thereby further erode the confidence in many of these outstanding programs.

Consequently it makes it possible for some to set up a straw man and to point to the delinquencies as a way to attack the underlying Government loan programs. We must vigorously pursue delinquent Government debt so as not to provide the opponents of programs, such as vital student loan programs, with reasons to oppose them. That is why you, Senator Percy, and I introduced legislation this morning to give Federal agencies the authority to contract out for the litigation of Government debt cases. This will put teeth in debt collection law.

Mr. Chairman, let me again commend not only you but a very fine professional staff that you have that has been in the fields doing the people's work. I am delighted to be able to participate in today's hearings with you.

[The prepared statement of Senator D'Amato follows:]

PREPARED STATEMENT OF SENATOR D'AMATO

Mr. President, today I am introducing legislation, the Federal Debt Recovery Act, along with my good friend and colleague from Illinois, Senator Percy, which will add an essential element to the arsenal of Federal debt collection. The measure we are introducing will authorize the heads of the various Federal agencies to contract with private law firms for the litigation of Federal government debt.

A recent GAO report states that "debts owed the government are enormous and growing each year, with billions of dollars delinquent." Federal agencies have reported that at the start of Fiscal Year 1982, over $33 billion in receivables due the United States government was delinquent. This delinquency rate represents a 37 percent increase over Fiscal Year 1980. Non tax delinquencies amounted to over $13 billion.

The GAO, in its report, finds that improvements have been made in the collection of federal debt in various Federal agencies. However, much remains to be in this area.

An understanding of one Federal agency, the Department of Education, and its efforts to cope with over $1.5 billion in delinquent Federal student debt provides clear testimony to the need for further strengthening the tools of Federal debt collection and the necessity for the legislation which we are introducing today.

There is currently somewhere between $1.5 and $1.7 billion in outstanding student debt owed to the Federal government. This debt consists primarily of defaulted National Direct Student Loans and Federally Insured Student Loans. This awesome amount owed to the Federal government does not include the approximately $200 million per year which the Department of Education is currently reimbursing state guarantee agencies for defaulted Guaranteed Student Loans. When this sum is considered, the aggregate student debt grows substantially in magnitude.

In 1982, however, despite a concerted effort, the Department of Education was only able to collect $55 million of this outstanding debt. The Department projects collections of $70.6 million this year.

On October 25, 1982, the President signed into law the Debt Collection Act. Among other things, the Act allows Federal agencies to charge interest and penalties on delinquent debt, offset the salaries of Federal employees having delinquent debts to the government, report delinquent debtors to credit bureaus and use private sector contractors to collect debts owed to the government. I commend Senator Percy, chairman of the subcommittee which oversees government debt, for this landmark piece of legislation and for his persistence in ensuring the promulgation of regulations which will implement this Act.

Examining the situation at the Department of Education, it is becoming very apparent, however, that an additional tool is necessary to adequately address burgeoning government debt, and that is the ability to use outside private attorneys to litigate cases.

Pursuant to the authority granted in the Debt Collection Act of 1982, the Department of Education referred 401,502 student accounts to private collection agencies. The dollar amount of this volume totalled $636.7 million. As of April 30, 1983, only $19.7 million, or 3 percent, of this sum has been collected by the collection agencies. The collection agencies themselves have recognized that the inability to threaten litigation or bring these cases to litigation dramatically undercuts their effectiveness. As the recent GAO report states, "contractors contend that this inability to bring suit generally hinders their collection efforts because they are deprived of one of the most important tools available to private collection agencies."

The Department of Justice simply does not have the capacity to handle the massive number of cases which the Department of Education and other Federal agencies will refer to it. For example, I recently asked the Department of Education to canvass the collection agencies with which it does business in major metropolitan areas and report back with an approximate number of cases which could be brought to litigation within a reasonable amount of time if the capacity existed at Justice. Education responded that over 26,000 cases could be called back from the collection agencies and litigated. The Department of Justice simply does not have the wherewithal—in particular a developed computer system—which could deal with this volume within a reasonable time frame.

In addition, there are serious questions as to the cost effectiveness of the Department of Justice litigating Federal debt. For example, according to Department of Justice statistics, student debt represents 22.8 percent of the debt case load at the Department of Justice. However, the dollar volume on this case load represents only 3.8 percent of all loans which have been referred to the Department of Justice by all Federal agencies for action. It would make more sense to turn these cases over to the private sector for litigation. Moreover, the opportunity costs of pursuing these cases which average only $1200 is great. The Department of Justice simply has too many other pressing matters to handle.

Department of Education records reveal that of the over $61 million that has been referred to the Department of Justice for action, only $4.6 million or 7.5 percent has been collected. The situation is much worse with regard to debt which has been turned over by other Federal agencies. Federal agencies must have the ability to contract out to private law firms for litigation services. Just as in the case of the private collection agencies, a contingency fee arrangement will provide these firms with a ready incentive to seriously collect government debt.

Senator Percy and I have been working for some months now with the Department of Justice and the Office of Management and Budget on the concept of litigating out government debt. We have also been dealing extensively with the Department of Education which has endorsed this concept. We are sensitive to the concerns which the Department of Justice has expressed regarding the need to oversee any litigation which is done for the United States government. We have accordingly incorporated necessary safeguards in this legislation. The bill permits the Attorney General to withdraw any of the cases contracted out by Federal agencies to a law firm if doing so is in the public interest. In addition, a law firm which is engaged by a Federal agency will be subject to the provisions of the Debt Collection Practices Act. Among other things, this Act prohibits a debt collector from harassing or abusing debtors, making false or misleading representations in connection with the collection of debt, and using unfair or unconscionable means to collect or attempt to collect debt. Finally,

a law firm doing business with a Federal agency must submit monthly reports to both that agency and the Department of Justice on the services rendered under the contract during the month and the progress made in the collection of the debt under the contract.

Mr. President, as a United States Senator I have been very supportive of many of the government loan and loan insurance programs. With regard to education, for example, I have been a staunch advocate of student financial assistance and believe in a strong Federal commitment to higher education. Every dollar which is not collected in student debt deprives a well-deserving student the right to pursue a higher education. The fact is that today many students and others who are receiving government loans are making a calculated decision not to repay their loans to the Federal government, convinced that the government has neither the inclination nor the capacity to recover the debt. Enactment of this legislation will provide an essential tool to Federal agencies to collect this debt. Moreover, it will just as importantly send a message to government debtors that the Federal government is serious about recovering monies which have been lent to them.

I urge the Congress to expeditiously pass this measure.

Senator PERCY. Thank you very much indeed. I would like to refer to the charts here which refer back to the hearings we held in December 1981 on the health profession student loan program so that we can see the dramatic reduction in delinquencies by universities. I selected these areas not because they are the largest loans, but because we do know that they are loans that go to people who have no trouble—that I know of—getting employment in this particular field. They are all professionals that are instantly hired and they go to relatively high paying jobs as compared to other student loans.

This pattern of improvement is the pattern that we hope will be followed by universities across the country. I think it will.

Our first witness today will be Harold Steinberg, Associate Director for Management, Office of Management and Budget, accompanied by Jack Donahue, Director of OMB's debt collection project. I would like to welcome you, gentlemen, this morning. Just over 2 years ago you sat before the committee with David Stockman, I believe. At that time, as part of the new administration, you were projecting that with new legislation and an all-out administrative effort over $1 billion, you said, could be returned to the Treasury in 1982. Now, after all of your hard work and a new law on the books, we will hear that this administration has far exceeded its original goal.

I commend you for this achievement. I know you have a strong background in accounting from your private sector experience. So you understand the importance of making the business end of government more business like. I look forward to your testimony.

TESTIMONY OF HAROLD I. STEINBERG, ASSOCIATE DIRECTOR FOR MANAGEMENT, OFFICE OF MANAGEMENT AND BUDGET, ACCOMPANIED BY JACK DONAHUE, DIRECTOR, DEBT COLLECTION PROJECT, OFFICE OF MANAGEMENT AND BUDGET

Mr. STEINBERG. Thank you, Mr. Chairman.

First I would like to introduce Jack Donahue, on my right, who is the director of the debt collection project.

Mr. Chairman, we are pleased to be here today to discuss the status of the debt collection project. I know you were right when you said that $2.1 billion more was collected than would have been collected in the absence of our aggressive program. But we think we can do even

better. We commend you, Senator Percy, and the committee, for the role that you have played in the past in the passage of the Debt Collection Act of 1982. We think it will enable us, indeed stimulate us to do better.

The first chart, I am sorry it is not in brilliant color as the other charts but it does show $2.1 billion that we have been able to return to the Treasury that we would not have been able to do if we had not started the debt collection program in the beginning of 1981.

Let me be a little bit more specific. As I indicated, $2.1 billion shows what the agencies were able to do once we instituted a program to encourage them to go out and collect the debt that was out there. When we saw that we were able to collect that $2.1 billion we set a more ambitious target for the fiscal year 1983 of $2.8 billion. Our 1983 preliminary numbers show that we will not only reach that target, but may exceed it. We needed to collect $1.2 billion in the first 6 months of this fiscal year to reach that $2.8 billion. We have actually achieved $1.4 billion in the first 6 months of this fiscal year. I think there is some other good news, too, as far as debt collection is concerned. Our total debt was increasing at an average annual rate of 18 percent prior to 1981.

In 1982, we were able to lower that increase to 13 percent and so far in 1983 we seem to be bringing it down even further. Comparing the first 6 months of 1982 to these first 6 months of 1983 the total debt grew at a rate of 5 percent and 3 percent respectively. So again we are slowing the growth of our debt. The delinquencies are also decreasing. Our delinquencies for the first half of 1983 are actually down by $500 million. We feel that in the last 6 months of the year, as the tax returns start to be filed, that number may go up slightly, but only slightly.

We will probably end the year with about $39 to $40 billion of delinquent debts.

Senator PERCY. Mr. Steinberg, could I ask if you could summarize your statement in about 10 minutes?

Mr. STEINBERG. Oh, yes.

Senator PERCY. We have a long list of witnesses today. Thank you.

Mr. STEINBERG. I am sorry. I should have said I was planning to summarize.

Let me talk just briefly about what we have done to implement the Debt Collection Act. Since the President signed the legislation last October we have established minimum interest rates to be assessed on delinquent debts of 13 percent. We have identified agencies and programs which can require credit applicants to furnish the taxpayer identification numbers and to screen loan applicants against the IRS files of delinquent taxpayers. Indeed the agencies are starting to do that.

We have issued the guidelines that explain the requirements of the Privacy Act under the Debt Collection Act so that the agencies can start to release the names of delinquent debtors to credit bureaus. We have provided the policies and procedures to guide the agencies in requesting IRS addresses and tax delinquent information. GAO and Justice issued the revisions to the Federal claims collection standards which provide Government-wide guidance for implementing the Debt Collection Act.

There remain some unresolved questions that have to do with Federal employee salary offset that will be published by OPM in subsequent regulations in the very near future. Then finally, in March we issued OMB Circular 83–11 to require the agencies to update their debt collection plans and include the major milestones for implementing the act. The initial review of the agencies' plans indicate that the agencies are already taking the steps to implement the act.

The Education Department, for instance, expects to be able to refer a minimum of 500,000 delinquent student accounts to credit bureaus in the next year. They published just yesterday in the Register the regulations that will describe the salary offset procedures for the 47,000 Federal employees that owe the Government $69 million in education loans.

But we don't want to declare victory as you indicated we could. The debt on those charts is quite large. We feel that in order to get it down and to keep it down, we must take steps that will have a significant and lasting impact on debt collection.

What I mean is that we must institute effective, businesslike procedures to prevent further delinquencies.

As you know, Mr. Chairman, Reform 88, the administration's management reform program will seek fundamental changes to assist in the policies that we are using to extend credit and collect debt.

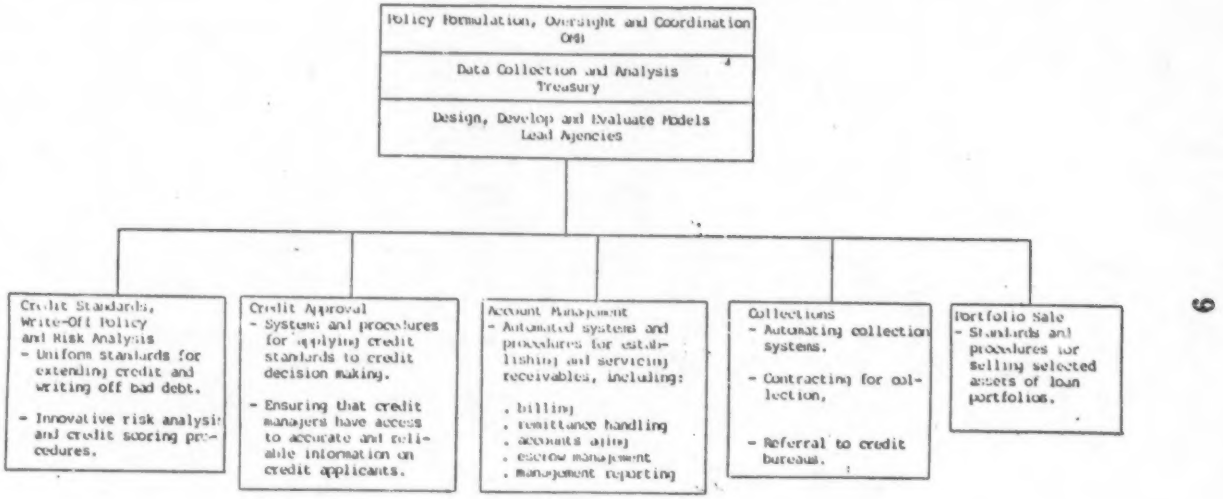
We have established five prime credit management areas in which we think we need to institute permanent change. The first is credit standards; the second is the credit approval process; third is account management; fourth is improved collections; and, fifth is the sale of portfolios.

I would like to introduce to the record an organization chart that indicates the assignments to certain lead agencies to effect these permanent changes in the Federal Government, and second, the identification of the problems and the deliverables that each of these agencies will be bringing to us over the next 2 to 3 years in order to bring about these permanent changes.

Senator PERCY. It will be incorporated in the record.

[The information referred to follows:]

REFORM 88
CREDIT MANAGEMENT INITIATIVES


Policy Formulation, Oversight and Coordination
OMB
Data Collection and Analysis
Treasury
Design, Develop and Evaluate Models
Lead Agencies
Credit Standards, Write-Off Policy and Risk Analysis
- Uniform standards for extending credit and writing off bad debt.
- Innovative risk analysis and credit scoring procedures.
Credit Approval
- System and procedures for applying credit standards to credit decision making.
- Ensuring that credit managers have access to accurate and reliable information on credit applicants.
Account Management
- Automated systems and procedures for establishing and servicing receivables, including:
. billing
. remittance handling
. accounts aging
. escrow management
. management reporting
Collections
- Automating collection systems.
- Contracting for collection.
- Referral to credit bureaus.
Portfolio Sale
- Standards and procedures for selling selected assets of loan portfolios.

Treasury	VA (Individual loans) Commerce (business loans)	Agriculture (in house)	Education (individual debts) SBA (corporate debts) Treasury (automated systems)	Commerce

CREDIT MANAGEMENT PROJECT ANALYSIS

Credit Standards

Problems:

- Government's role as "lender of last resort" results in more lenient and flexible standards than those used in the private sector.
- Terms and standards are usually set by statute without regard for the impact on collection practices or resources

Remedies:

Uniform credit standards

Credit Review and Approval

Problems:

- Agencies do not make use of risk analysis techniques or loss-rate goals to control losses and determine resource needs
- Insufficient information on the credit worthiness of applicants results in bad credit decisions

Remedies:

Minimum standards for individual and commercial loan applicants

National Credit Information System

Standardized applications/ modifications of existing applications

Automated system for credit approval and credit scoring

Risk analysis and credit scoring procedures govt.-wide

Account Management

Problems:

- Accounting systems are incapable of supporting effective debt servicing and collection
- Supporting records systems are generally not automated and do not provide reliable information on the condition of debt portfolios

Remedies:

Implement automated system for servicing receivables in high and low volume debt agencies

Debt Collection

Problems:

- Cost/benefit analyses to determine level of collection activity not performed
- Credit bureaus are not used
- Private collection firms are not used
- Agencies do not take advantage of offset possibilities to recover delinquent debt.

Remedies:

Contract out collections

Portfolio sales begin

IRS collection system in place

User agency collection system in place

Write-off

Problems:

- Write-off policy varies from agency to agency
- Agencies are unwilling to classify debts as uncollectible

Remedies:

Government-wide write-off criteria implemented

Mr. STEINBERG. Basically, we are asking these lead agencies to develop models that would be applicable throughout the Government. For instance, the Internal Revenue Service is in the process of developing an automated collection system for managing the portfolio and collecting the debt.

The IRS has already initiated a pilot system that is fully automated and we are looking to see whether or not similar systems can be used for the collection of nontax debts by other Federal agencies.

One thing that you alluded to in your opening statement which I would like to comment on is the need for increased litigation of delinquent debt cases.

Justice today will be proposing that the Attorney General be given the authority to retain private attorneys for handling litigation of claims referred to Justice under the Debt Collection Act.

We endorse this concept. We look forward to working with the committee to secure passage of the necessary legislation. Indeed, we think there are still a number of legislative solutions to improving the debt collection programs.

We know that the Senate passed S. 376 last week which will permit payment of collection agencies from proceeds of debt collection and we look forward to favorable consideration of that bill within the House.

So, Mr. Chairman, I believe we have established the solid foundation to sustain long-range improvements in debt collection and with your consideartion and support, the efforts that we have made to date will be continued, expanded, and intensified.

I would be glad to answer any questions that you may have.

Senator PERCY. Thank you, very much, indeed.

We have the report from the GAO of April 26, 1983, and certainly your own testimony today indicates that we have made dramatic headway, double the figure that you, yourself, mentioned.

I think I told you at the time years ago that I had set a rather unusual goal for my Senate staff. I came in my office when I came down here in 1967 and said, "Look, you are a load on the taxpayer's back unless you pay for yourselves."

I never had been in a business where I didn't see every single worker in that business had to be far more productive than earning the salary. They had to earn the salary, plus the overhead, plus return on investment and everything else. This is a business.

I didn't know how to run anything but a business. So everyone had to think what they could come up with as ideas. What we set as our goals was to save my salary, which was, then, $30,000 a year, every single legislative day of the year. We quickly changed that to the total expenses and salaries of everyone on our staff and we have returned all of it since that time. It has gotten so big we really stopped accumulating the figure. Here you have another pickup of $2 billion and $3 billion next year. That is a pretty good return on our investment. So I don't have to apologize about trying to get a salary increase around here sometime. [Laughter.]

Mr. STEINBERG. You may want to get more staff, too.

Senator PERCY. But we have had one area of disappointment. It has taken longer than we had hoped to implement the Debt Collection Act.

It has taken 7 months to issue the regulations putting the act into effect. This delay has cost taxpayers hundreds of millions of dollars.

Just last week, the regulations were published. It is crucial that the act now be implemented swiftly.

Could you tell us how long it will take to begin using credit bureaus and charge interest penalties? That is the thing that will do more to cause people to pay—when they see that on a utility bill, unless you pay this by such and such a date, it is going to be this much more.

What motivates them to pay? They hate utilities. But they hate to pay a penalty. They are going to pay it ahead of time. We have got to do the same thing. This delay is unnecessary, I think. If you could tell us, then, how long will it take to get into using credit bureaus, charging interest penalties and putting into effect the other tools that are provided by the act?

Mr. STEINBERG. As far as the use of credit bureaus is concerned, we have been negotiating with companies in the private sector to set up a national credit bureau system that all of the agencies will be able to file consistent information with credit bureaus. We hope to have a GSA contract with the credit bureaus to enable agencies to obtain reports from the credit bureau and avoid the need for each agency to contract.

We think that will facilitate the process quite a bit. We are shooting for an implementation date at the end of this calendar year with the National Credit System. In addition, agencies are taking advantage of the new authority to charge interest.

I think we will start seeing results by the end of this fiscal year.

Senator PERCY. Very good. When I felt the Department of Education under Secretary Bell needed a shot in the arm, I went over to talk to him. We spent a couple of hours over there talking with the people in charge of the program and addressing a very large group of people.

I think there was action as a result of this meeting. Any time I can, I personally go over and say, look, OMB has got a tough enough job. They are carrying out a mandate from Congress; we are the bad guys, if you think we are putting on too much pressure. But I will be happy to go over and deliver that message personally.

I am sure that Senator D'Amato would join me anytime that it affects the interest that he is following.

Mr. STEINBERG. I appreciate that.

Senator PERCY. As I indicated in my opening statement, one of the major weaknesses remaining in our collection efforts is the litigation of defaulted loans. There is literally $700 million going uncollected for lack of litigation.

In this hearing, we are going to hear evidence that points to the need to allow the Government to contract with private law firms that specialize in collection litigation.

Does the administration fully support using private litigation and would you endorse legislation such as Senator D'Amato and I are introducing, allowing private litigation?

Mr. STEINBERG. Yes, sir, the administration does support that legislation.

Senator PERCY. Very good. I very much appreciate that position being made. That will help our legislation, I think, speed through the process.

The Department of Education is going to testify today that most of the gains they have made in collecting defaulted student loans are attributable to the use of private collection agencies. Almost every private sector retailer credit card company and major corporation uses a private collection agency. Though you wish you could do it internally, the business sector has found they just don't have the resources, they don't have the skill to do it.

A private collection agency does have it. The Small Business Administration, Veterans Administration, Department of Housing and Urban Development, had delinquent debts owed them which totaled almost $10 billion—just $10 billion in those agencies I have named.

SBA's delinquent debt increased almost 60 percent in 1 year. In spite of these tremendous backlogs of uncollected debts, these agencies steadfastly oppose using private collection firms. They say they are doing a good job on their own.

Why, in your judgment, are these agencies not taking advantage of collection agencies? Does OMB feel that these agencies should be using them more?

Mr. STEINBERG. I don't think it is a matter of steadfastly refusing as much as it is a matter of the facility with which they can use them. For instance, in HUD, they use the private sector agencies extensively for the account management work on the single family loan. They started a pilot project in region 3 in Baltimore last year and they are now considering expanding that to the rest of the country. The problem that a lot of the agencies had with contracting for collection is being able to pay the collection agencies out of the proceeds of the collections. Having the ability to make payment in this fashion would greatly stimulate and expand the use of the private sector collection agencies.

That is why we said I was glad to see that bill pass the Senate last week and I hope we will have quick passage in the House.

Senator PERCY. I have no questions for you, Mr. Donahue. I just want to welcome you to this job. You have replaced Jerry Bridges, who was OMB's No. 1 debt collector. His will be a hard act to follow. He set very high standards, and did a truly outstanding job.

I just want to assure you that I personally and our entire staff will give you all the cooperation that you need in this noble work that we are carrying on. I believe you are going to stay on top of the issue and I think your background eminently qualifies you to carry on an outstanding job.

Senator D'Amato?

Senator D'AMATO. Thank you, very much, Mr. Chairman.

Mr. Steinberg, it is always nice to have a fellow New Yorker before a Senate committee, particularly one who attended Syracuse University.

Let me commend OMB, which is something I do very rarely. If you see Dave Stockman, you say that I did that today. He won't believe it. It is very unusual. You tell him Senator D'Amato did commend OMB for undertaking these important initiatives.

I would hope that we will be able to work in implementing some of the legislative proposals. I am particularly gratified by your response to Senator Percy's question, his inquiry with respect to whether or not

you would be supportive of our legislative endeavor. So that I might hone in just a little bit, I understand that Justice and OMB have developed a proposal that varies somewhat from that which Senator Percy and I introduced. Essentially, your proposal would permit Justice, rather than the Federal agencies, to contract out for litigation services. Is that correct?

Mr. STEINBERG. The contracting out would be undertaken by the Justice Department. Yes.

Senator D'AMATO. Let me ask you why not the various agencies, for example, the Department of Education or HUD or the SBA people under the jurisdiction, under the pervue obviously of the Justice Department which would retain the ability to take back any case when it felt it was important to do so.

If you read our legislation, we provide for very careful and thoughtful oversight. What I am concerned about is the ability of the Justice Department to deal with these matters because in many cases they are of a secondary importance.

Given the activities and problems which come up at Justice, I am very much concerned that it will do less than a full and adequate job of collecting the bad debt, the moneys owed, that this would be a low priority item.

Let me make another suggestion. I think that possibly we might be willing to amend our language to provide that the Justice Department would have the right to review any of the recommendations for contracting out and within 30 days either approve or turn down the recommended law firm. And in this way, we would see to it that we would not have the kind of bureaucratic snafu with days gone by, weeks gone by, months gone by, and nothing done.

What do you think about that as a manner in which to address what I certainly know is going to take place, and that is, the bureaucracy just picking up a pile of paper at one desk and shifting it to another?

Mr. STEINBERG. I think there are really two pieces to making sure that the intention of the statute is carried out, one is the attitude of the agency and the other is the actual procedure. In terms of the attitude, I think that the Justice Department under this administration has gone after the debtor. I can't question it. I have been impressed by the top level people that have been assigned to the debt collection project, and the guidance that has been given to them by the Attorney General and the Deputy Attorney General. The Justice performance leads me and others in the administration to be convinced that the Department considers debt collection as important as many of their other responsibilities.

Having said that, we now need to look at what makes the process work best. It is my understanding that the way the Justice Department is looking at it is to be able to use these outside contractors in support of the U.S. attorneys and that would facilitate carrying on this litigation. Once the contract is let by the Department of Justice it could well be that the actual management of the process could be done by the involved Department. But I think you will hear more about the specifics of the proposal from the Justice Department.

Senator D'AMATO. Let me, just for the record, indicate that the Department of Education has, to date, referred $61 million to the

Justice Department for action and Justice has collected $4.6 million, or 7.5 percent. Obviously this is not a high priority item. Obviously it is not a coincidence that Justice comes forth today with a proposal after 3 months of staff and committee begging, cajoling, and exhorting; that it comes forth in this manner and we finally hear, oh, yes, we will go forward, we will support legislation that will put teeth in debt collection.

So I must suggest to you that this is one Senator who is somewhat suspect and who views the Justice Department as somewhat reluctant. You know you can lead a horse to water but you can't often make the horse drink. So I don't intend to get involved in that kind of situation. Therefore, I would suggest to you very carefully, that in order to see that we don't have the kinds of snafus, that there be an amendment in our legislation that says that within 30 days Justice either approves or disapproves a law firm for undertaking debt collection.

If we are serious about it, we are not going to have these battles over turf. If Justice wants to call the lawyer from the firm a special U.S. attorney, so be it. If that is what makes it happy, good, we will put that in there. We will designate him a special U.S. attorney. How does that strike you?

Mr. STEINBERG. We will take a look at that proposal. [Laughter.]

Senator D'AMATO. Thank you very much, Mr. Chairman.

Senator PERCY. We thank you, Mr. Steinberg, and Mr. Dohahue, very much indeed. We appreciate your full cooperation.

[Mr. Steinberg's prepared statement follows:]

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

STATEMENT OF HAROLD I. STEINBERG
ASSOCIATE DIRECTOR FOR MANAGEMENT
OFFICE OF MANAGEMENT AND BUDGET
BEFORE THE
SUBCOMMITTEE ON ENERGY, NUCLEAR PROLIFERATION
AND GOVERNMENTAL PROCESSES
OF THE
COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

MAY 25, 1983

Introduction

Mr. Chairman, I am pleased to appear before you this morning to discuss the status of the Administration's efforts to improve the collection of debts owed the Government. In FY 1982, $2.1 billion more was collected than would have been collected in the absence of our aggressive debt collection program. The increased collections were the result of a wide range of administrative reforms which agencies instituted to improve their credit management and debt collection practices.

Before reviewing this progress in greater detail, however, I would like to express my appreciation for the cooperation and support which we have received from this Committee. Your active interest in improving the Government's debt collection program was instrumental to the passage of the Debt Collection Act of 1982. Thanks to your tireless efforts, we now have legislation which significantly expands the variety of debt collection tools and techniques at our disposal. I will describe shortly how we are

using these newly available tools and techniques. But first I want to report our progress for the first half of this year.

Increased Collections

As you know Mr. Chairman, an important element of our debt collection program has been to establish collections targets for those agencies with significant amounts of debt. The targets represent collections over and above what would normally be collected by agencies in a given year. At the beginning of FY 1982, we established increased debt collection targets totaling $1.5 billion. Based upon our analysis of final FY 1982 data, we have determined that, in fact, an additional $2.1 billion was collected in FY 1982. In other words, Mr. Chairman, we exceeded the projected target by $600 million. We have depicted the accomplishment on a bar chart, which I would like to include in the record.

Based upon this success in 1982, we have established even more ambitious targets for 1983 and 1984. The President's 1984 Budget reflects debt collection targets in excess of $2.8 billion for 1983 and $3.2 billion in 1984. After completing an analysis of preliminary mid-year data, I am pleased to report that we are well on our way to achieving the $2.8 billion target. Specifically, we had projected that collections in the first six months of 1983 would have to increase by over $1.2 billion. The

preliminary data available to us indicates that collections have actually increased by over $1.4 billion.

In addition to increasing collections, Mr. Chairman, we are also having an impact on the growth in total debt owed the Government. Prior to 1982, total debt had increased at an average annual rate of 18 percent. For 1982, that rate of growth was slowed to 13 percent, as total debt grew from $241.5 billion to $273.2 billion. In the first six months of 1983, it appears that the rate of growth continued to decline. Total debt owed the Government increased only 3 percent in the first six months of 1983, to $282 billion, while the increase for the comparable period in 1982 was 5 percent.

With respect to delinquent debts, we experienced a decrease of nearly $500 million in the first six months of 1983. The decrease is due to the success which IRS has had in collecting delinquent tax debts. We expect that tax delinquencies will rise somewhat in the second half of the year, as the processing of 1982 returns is completed. However, the increase should not be significant, and at the end of 1983, delinquent tax debts should

be at approximately the same level they were at the close of last year.

Implementation of the Debt Collection Act of 1982

Let me turn now to the steps we are taking to implement the Debt Collection Act of 1982. As I stated earlier, we believe the Act will enable us to further improve our debt collection efforts. The authority to contract with experienced private firms for the collection of Government debts and to refer information on delinquent nontax debts to credit bureaus, along with the other powerful debt collection tools provided by the legislation, will greatly expand our ability to collect our debts efficiently and effectively.

The President signed the legislation in October. Since that time we have been working closely with the agencies to put the Act in place across the Government. Specifically, the following steps have been taken:

- We have established the interest rate to be assessed on delinquent debts (13 percent);

- We have identified the agencies and programs which can (1) require credit applicants to furnish their taxpayer

identification numbers, and (2) screen loan applicants against IRS files of delinquent taxpayers;

- We have issued guidelines explaining the relationship between the new legislation and the Privacy Act; and

- We have established policies and procedures for agencies to use in requesting IRS address and tax delinquency information.

Another important step in implementing the Act is the issuance of revised Federal Claims Collection Standards. The Standards, which are the responsibility of the General Accounting Office (GAO) and the Justice Department, are used to provide government-wide guidance on the provisions of the legislation. The issuance of the Standards had been delayed because of some unresolved questions concerning the due process which must be provided to debtors in the case of judgment debts and routine overpayments of pay which result from clerical or administrative errors. I understand that because of the urgency of providing guidance to the agencies, the GAO and the Justice Department have agreed to publish proposed Standards which do not address this issue, and to work with the Office of Personnel Management (OPM) to resolve the remaining differences on the due process issue.

One final element of our implementation efforts is OMB Bulletin No. 83-11. The Bulletin, which was issued on March 1, requires agencies to update their existing debt collection plans to include major milestones and target dates for implementing the provisions of the Act. Our review of the plans submitted to date indicates that agencies have already taken steps to make use of the powerful tools provided by the Act. For example, the Department of Education has initiated a major effort involving the referral of information on delinquent student loans to credit bureaus. Beginning in June, approximately 50,000 delinquent student loan accounts will be referred to credit bureaus. If there are no problems with the tape-to-tape transfer of the delinquent debt information, the Department expects to be able to refer a minimum of 500,000 delinquent accounts in the next year. We feel this activity is an important step in the Department's efforts to recover its delinquent student loans.

We are also seeing increased activity in the area of contracting with private firms for collection services. Earlier this month, the Air Force initiated a pilot program to test the cost effectiveness of using commercial collection agencies to supplement their own debt collection efforts. Contracts for the collection of delinquent out-of-service debts were awarded to two firms. An estimated 8,000 delinquent accounts valued at $1.6 million are expected to be referred to the contractors in the first year of the program. The debts will be referred to the

contractors after all internal Air Force collection efforts have been exhausted.

Future Directions

Mr. Chairman, I have discussed what I feel to be some significant accomplishments in debt collection. But our debt collection problems are by no means licked. I am convinced that if we are to have a significant and lasting impact on the Government's debt collection efforts, we must make fundamental changes to the policies and procedures used in extending credit and collecting debt. Our mission is, therefore, twofold. We must:

- Continue our aggressive action to recover existing delinquencies, and

- Institute effective and business-like policies and procedures to prevent unnecessary new delinquencies.

Because of the enormity of this task, we have made improved debt collection a key element in Reform '88, which is the Administration's major initiative to restructure the management and administrative systems under which the Government operates. The Reform '88 agenda for debt collection is specifically designed to meet our dual mission. For example, the management information systems in most agencies currently lack automated systems support,

provide limited data on the condition of agency debt portfolios, and frequently cannot support essential credit management and debt servicing and collection functions. To address these deficiencies, we plan to develop automated systems for managing debt portfolios and collecting Government debts. These systems will ensure that agencies have accurate and reliable information for debt collection purposes.

In this regard, I would like to relate the innovative steps being taken by IRS to improve their collections performance. On May 9, IRS initiated a pilot test of an automated system for the collection of delinquent tax debts. The automated system, which will be used after initial collection efforts have proven unsuccessful, will replace paper files and manual processes and tracking systems with a fully automated office environment. If the pilot test proves successful, IRS will have the system installed throughout the country. This will occur by next summer. In the long run, IRS will be able to use fewer people to collect more money more efficiently. Because of the implications the IRS system has for the collection efforts of other agencies, we are investigating whether similar automated systems can be used for the collection of nontax debts.

We have also found that many agencies still do not have consistent policies for the performance of such essential functions as credit scoring and risk analysis, collecting

delinquent accounts, and writing-off bad debts. Under Reform '88, we will develop:

- Risk analysis and credit scoring procedures which ensure the integrity of the credit extension process;

- Standard procedures for using a variety of collection practices to improve the collection of delinquent debts; and,

- Government-wide criteria for writing-off bad debts.

Mr. Chairman, I am also aware of your concern over the Government's ability to aggressively prosecute those debt cases for which agency collection efforts have proven unsuccessful. I understand that this morning the Justice Department will propose that the Attorney General be given authority to retain private counsel for the purpose of handling litigation to collect claims referred to the Justice Department under the Debt Collection Act of 1982. While I will let the Justice officials outline their proposal in greater detail, let me assure you that we endorse the concept of using private attorneys to supplement the Governmment's litigation efforts and look forward to working with you to secure the enactment of the necessary legislation.

Future Prospects

Mr. Chairman, I am convinced that the progress which I have reported today provides a solid foundation for sustained, long-range improvements to the systems and practices which the Government uses to collect its debts. I might also point out that the General Accounting Office (GAO) has reached a similar conclusion after reviewing our debt collection program. In the report issued following its review, the GAO concluded that the prospects for further improvements in debt collection look good for fiscal 1983-1985.

As I have also pointed out, however, there is considerable work remaining. This Administration is firmly committed to meeting these challenges in order to ensure that the Government's debt collection program operates on a sound, business-like basis. With the continuing cooperation and support of the agencies and Congress, I am positive that the efforts we have made to date will be expanded and intensified.

Senator PERCY. Our first panel this morning is Roger Feldman, Comptroller, Mr. Charles Koeneman, Chief of the General Accounting Division, and Ms. Ann Swift, Acting Chief of the Citizens' Emergency Center, from the Department of State.

I want to welcome today these representatives from the State Department. I have met with Roger Feldman, the Comptroller, on other occasions. Mr. Koeneman and Ms. Swift, we welcome you. The State Department has come here this morning to discuss with us their repatriation loan program, a small but necessary State Department program which provides loans to U.S. citizens who find themselves in foreign countries without financial means to return to the United States.

When I first looked into the program 2 years ago, it had one of the highest default rates of any Federal loan program. The reasons for this were obvious. For example, borrowers were not even asked for their social security numbers, no interest was assessed on overdue accounts, no deadline was ever placed on the time they were to repay the loans and relatives who might have been able to pick up the bill were not even contacted.

It was embarrassing for them but not too embarrassing to come to ask their Government to bail them out, to get them back from Europe, or whatever foreign country they happened to be in. But they needed money to get home. We don't need that much stimulation to the economies abroad. They can't even keep enough money to get back home on. I understand major improvements have been made in the way the repatriation loan program is administered and the collection records have improved dramatically recently. Mr. Feldman, we look forward to hearing your testimony at this time. We take this case as a small case, but a case where the principle is established. We are going to do something about this.

The Department sets out the problems, say this is a part of our problem and we are going to do something about, to make this program a credible, sensible program that we can justify to our taxpayers. You have done that, I think.

TESTIMONY OF ROGER FELDMAN, COMPTROLLER, DEPARTMENT OF STATE, ACCOMPANIED BY ANN SWIFT, ACTING DIRECTOR, CITIZENS EMERGENCY CENTER, DEPARTMENT OF STATE, AND CHARLES F. KOENEMAN, CHIEF OF THE GENERAL ACCOUNTING DIVISION, DEPARTMENT OF STATE

Mr. FELDMAN. Thank you, Mr. Chairman.

I am pleased to appear before you today, Mr. Chairman, to discuss the improvements that we made in the Department of State in limiting the number of loans and improving our collections in the repatriation loan program.

I have with me this morning Ms. Ann Swift, on my right, Director of the Citizens Emergency Center in our Bureau of Consular Affairs, and Mr. Charles F. Koeneman, Chief of our General Accounting Division.

Our repatriation loan program has, since at least 1942, provided emergency extension of credit for the cost of a one way airline ticket

back to the United States for destitute U.S. citizens stranded overseas. Whenever possible, our consular officers obtain reduced rates and standby airfares, often half the cost of conventional full fare coach seats. Each repatriate's passport is limited to return to the United States and the Department will not issue another passport until the loan is repaid.

The Department attempts to contact relatives and families to see if they can provide funds. A recent study by our Consular Affairs Bureau covering a 7-month period indicated that through contacting relatives or friends, 58 of 729 repatriation loan applications, adding up to $38,000, were resolved by these families or friends transmitting airfare funds overseas.

The Department of State supports Public Law 97–365, the Debt Collection Act, and even before its passage took positive steps to improve our debt collection program. Since May 1981 we have required loan applicants to provide their social security numbers. We have instituted provisions for repayment of loans with interest, as opposed to interest free loans which existed for a number of years.

Further, we inform each applicant that payment in full is expected in 60 days or interest commences at the current Treasury cost of borrowing. The Department has accelerated our billing process by requesting posts to report loans telegraphically as soon as they are extended. In addition, we obtained an exemption to the "Fly America Act" which has enabled our embassies and consulates to repatriate U.S. citizens at the least cost to the U.S. Government.

The Department is pleased to report the worldwide collections of repatriation loans increased 8 percent and the amount of new loans decreased a similar 8 percent in fiscal year 1982 as opposed to fiscal year 1981. Specifically, collections improved to $270,000 in fiscal year 1982 over the $253,000 collected in fiscal year 1981. Similarly, the dollar value of loans extended was reduced from fiscal year 1981's $620,000 to fiscal year 1982's $575,000 although the number of loans granted increased slightly from 1,620 to 1,650 during this period. The average loan in 1982 was $349 compared to $275 10 years ago.

The Department is currently using IRS project 719 for obtaining current addresses and has obtained over 500 addresses for old accounts from the IRS for billing purposes. We have also exchanged addresses with VA and HHS to obtain addresses from those agencies for which our application forms indicated that the applicant was eligible for benefits.

On a test basis we have placed some of our delinquent, written-off accounts with collection agencies in Pennsylvania, New Jersey, and South Carolina. We have had limited success with this program, having collected on 5 of 31 of these accounts or on $2,000 of the $35,000 placed with these agencies.

Mr. Chairman, we will be pleased to answer any questions you and the committee may have.

Senator PERCY. I do have a few. Meanwhile, I would like for John Kelso, Deputy Administrator, Health Resources and Services Administration, Department of Health and Human Services, and Robert Webber, General Counsel to the Small Business Administration, to join us at the table.

First, I do want to commend you for your efforts in this area. I think we both agree the repatriation loan program still has a disturbingly high default rate.

How many of these cases have you referred to the Justice Department for litigation?

Mr. FELDMAN. One case, Mr. Chairman.

Senator PERCY. What is the reason that no litigation was requested in the case of others? Was it simply that the resources of the Department are inadequate to collect?

Mr. FELDMAN. Mr. Chairman, the problem that we encountered, as you are aware from our program, is that the amount of our dollar value per loan is very low. It is our understanding that Justice is not inclined to accept a case that is below $1,200.

Since our average loan is only several hundred dollars, we don't often reach the threshold for the Justice Department to undertake litigation.

The one case that we did refer to them within the past year was an organized tour from Boston and the total of that case is about $14,000.

Senator PERCY. Do you have any reason to believe that it would be impossible to find offsite collection agencies, even though they may charge 25 percent, to take such cases?

Mr. FELDMAN. No, Mr. Chairman. It is my understanding from the people involved in that aspect of litigation that they have the skills and techniques if given sufficient volume to pursue those cases. We would support that.

Senator PERCY. Does the State Department have the authority now to hire outside collection agencies or law firms to bring litigation?

Mr. FELDMAN. I don't believe that we have the authority to hire outside law firms, Mr. Chairman.

Senator PERCY. You do not have the authority?

Mr. FELDMAN. No, sir.

Senator PERCY. That is an issue we can discuss later. Perhaps you can take this time to describe the case in Boston, the one case which Justice did accept.

Mr. FELDMAN. Mr. Chairman, I will have to paraphrase because we have submitted this case to the U.S. attorney in Boston and are awaiting his action, hopefully, to pursue it in the courts.

There was a group of 16 adults and 106 minors from a northeastern inner city who went overseas to Europe on an organized tour to perform as a marching band. They went from New York to Brussels on Metro Airways, a subsidiary of Flying Tiger Airlines. I believe some time after their arrival in Europe, the check that had been presented for the payment of their air fare bounced. They, then, proceeded to tour Europe, performing, and I think much in the hope of raising funds so that they could get back to the United States.

They finally made their way to Essex in the United Kingdom just outside of London, where they were bivouacked in a Boy Scouts camp and, of course, you know it is rainy and cold in the United Kingdom. They were destitute. They had no way of getting back to the United States. We had on our hands over 100 youngsters, one of whom had to be hospitalized for pneumonia, with no means to get back to the United States.

I must say that our consular officers performed heroically, I believe, in this instance and managed to arrange for some of the group to receive passage on Northwest Airlines to return to the United States.

We, then, proceeded to transport the rest of them back to Brussels where Flying Tiger Metro was willing to acknowledge a certain level of responsibility on their part and proceeded to take the rest of the group back to the United States at no charge.

We received a promissory note from the individual who had organized this tour and sponsored it, and that individual is the one whom we feel Justice should pursue prosecution against.

Senator PERCY. How much is that promissory note for?

Mr. FELDMAN. It is just shy of $14,000, Mr. Chairman.

Senator PERCY. When did you refer that case to Justice?

Mr. FELDMAN. October 1982, last October.

Senator PERCY. October of last year. This is the end of May.

What has happened since then? Have they filed a suit against the individual?

Mr. FELDMAN. No, Mr. Chairman, they have not. In December we followed up on the case and were told that an attorney and a case number had been assigned.

Our most recent contact is that they are in something referred to as presuit or preliminary collection work and that they may be filing suit sometime in the near future.

Senator PERCY. When the individual was contacted and advised that you had turned the case over to Justice, and was told to contact Justice, was there any contact by that individual at all?

Mr. FELDMAN. No, Mr. Chairman.

Senator PERCY. So there again, if he just waits it out, the Government will forget it, is probably his attitude.

Is the individual capable of raising that money?

Do you have any idea?

Mr. FELDMAN. I am afraid I don't know, Mr. Chairman, but from what I know about the case, I do not really see any indication that he could.

I must say, apropos of our earlier remarks about the private sector, that we do have another interested party, in that Flying Tiger Airlines also is owed a considerable amount of money; and, I believe, the figure is $72,000.

So I think that they will produce the case along as well. But progress is obviously not very vigorous at this point.

Senator PERCY. Senator D'Amato, do you want to ask any questions?

Senator D'AMATO. No.

Senator PERCY. I think we can excuse the three of you if you would like to go.

If you would like to stay here and hear the testimony of the remainder of the panel, you can certainly do that.

From the Department of Health and Human Services, we would like to welcome here today Mr. John Kelso, Deputy Administrator of the Health Resources and Services Administration, and Mr. Tom Hatch, Director of the Bureau of Health Professions.

I feel it is especially important to have the Department of Health and Human Services represented here today because, as I mentioned in my opening statement, about 1½ years ago, I chaired a hearing which focused on disturbingly high default rates within the Department's health professions student loan program.

Since that hearing, there have been dramatic improvements in individual school's collection records, and the overall delinquency rate has dropped from 15.2 percent in June 1981, to 11.7 percent in June 1982—a 23 percent reduction in delinquencies.

Mr. Kelso, I would like to commend HHS for making this issue a top priority. I look forward to your testimony at this time.

TESTIMONY OF JOHN H. KELSO, DEPUTY ADMINISTRATOR, HEALTH RESOURCES AND SERVICES ADMINISTRATION, DEPARTMENT OF HEALTH AND HUMAN SERVICES, ACCOMPANIED BY THOMAS D. HATCH, DIRECTOR, BUREAU OF HEALTH PROFESSIONS

Mr. KELSO. Thank you, Mr. Chairman.

Mr. Chairman and Members of the subcommittee, I am pleased to have this opportunity to testify before your subcommittee on the further progress that has been made in reducing delinquency under the health professions student loan program.

I am the Deputy Administrator, Health Resources and Services Administration, and I am accompanied by Thomas D. Hatch, Director, Bureau of Health Professions. Under last year's reorganization of the Public Health Service, the Bureau of Health Professions has carried forward the debt management efforts begun so effectively by the Bureau of Health Personnel Development and Service under Dr. Daniel F. Whiteside.

In my statement today, I shall review steps taken since your subcommittee's hearing of July 21, 1982, aimed at improving the management of the health professions student loan program. I shall describe reductions in delinquency rates that have occurred and report on the status of our efforts to collect loans overdue from employees of this Department and other Federal agencies.

First, I would like to recall for you the history of the loan program.

In 1963, the Congress authorized the health professions student loan program as part of an overall effort to meet a national shortage of physicians, dentists, and other health professionals.

Over the years, changes have been made in the types of institutions which were eligible to participate, amount of loans, rate of interest, and terms for repayment. However, as the program has evolved, its basic purpose has remained essentially unchanged: To enable health professions schools to provide long-term, low-interest loans to students in need of assistance to complete health professions training.

Under the program as most recently reauthorized by the Omnibus Budget Reconciliation Act of 1981, participating educational institutions may make loans to eligible health professions students for up to $2,500 a year plus tuition.

Medical and osteopathic students who receive awards must be of exceptional financial need. Interest is payable at 9 percent on the unpaid balance during a 10-year repayment period which begins after

the student completes academic training and certain periods of deferment for postgraduate education or other specified purposes.

To participate in the program, eligible schools apply to the Department for allocation of funds and then subsequently establish a Federal capital contribution fund for making loans to students.

Schools are required to contribute 10 percent of the total cost, with HHS contributing the remaining 90 percent. Principal and interest collected on loans are used by the schools to be reloaned to other students, hence creating revolving loan funds.

Since the beginning of the program, Federal contributions have totaled some $390 million. In recent years, appropriations have been reduced, dropping to $1 million in fiscal year 1983. New loans to students currently are being made primarily from collections from borrowers on previous loans—estimated to be about $38 million for the school year ending June 30, 1983.

As we have explained to your subcommittee at earlier hearings, the Department has responsibility for making awards to eligible institutions, developing regulations and policies for the participating schools to follow in the award and collection of loans, and monitoring schools' administration of the loan program.

As you recall, under current law, the Federal Government has no authority to collect money from individual borrowers, to have notes referred to the Federal Government for collection, or to select students who will receive awards.

On the other hand, the schools' responsibilities in administering their loan programs are quite explicit. They are responsible for selecting students for awards, processing promissory notes, counseling students on repayment obligations at the time awards are made, conducting exit interviews prior to students' graduation from the institution, maintaining contact with borrowers during the periods of postgraduate training when repayment has been deferred, and otherwise exercising due diligence in collection of outstanding loans.

Since our last appearance before your subcommittee, the Department has pursued a number of administrative initiatives to help assure that schools reduce loan delinquency. We have continued to provide assistance to schools in the form of site assessments which evaluate program operations, identify program strengths and weaknesses, and recommend needed changes in program administration. A total of 355 such assessments were made at health professions and nursing schoods in 1982. During fiscal year 1983, we will make an additional 355 assessments; to date, 184 have been conducted.

The Department is developing a revision in health professions student loan regulations to require more fiscal accountability at the institutional level and to improve monitoring and collection functions.

Published late last summer as a Notice of Proposed Rulemaking, these regulations would require that the schools maintain more rigorous recordkeeping and collection procedures and would establish performance standards against which a school's delinquency rates would be measured. The regulations will be signed by the Secretary and published in the immediate future.

In addition, the Department is developing proposed regulations to provide greater specificity for the determination of due diligence as required of the schools in program administration and loan collection.

The schools have urged the Department to clarify the standards by regulation. We hope to publish an NPRM by late summer. Similar rules will cover the nursing student loan and health education assistance loan programs.

To deal with schools where loan delinquency is a particular problem the Department has entered into a contract for the provision of technical assistance in the solution of debt collection problems at selected health professions schools. This is in addition to the assessment visits discussed previously.

During the current year, on a pilot basis, some 10 health professions schools will receive assistance with respect to accounting systems, billing procedures and cash flow, procedures for properly aging accounts, procedures for acceleration of delinquent accounts, development and use of demand letters, use of collection agencies, litigation procedures, State laws regarding debt collection practices, or preparation of necessary records and reports. In fiscal year 1984, an estimated 25 health professions schools will receive this assistance.

A system of quarterly reports from schools has been inaugurated. The reports, including information on delinquency rates, excess cash, and program accounts, were first collected for the period July 1–September 30, 1982.

Reports for the period October 1–December 31, 1982, also have been collected and reports on the period January 1–March 31, 1983 are currently coming in from the schools.

The automated quarterly reporting system has already expedited collections of excess cash from the schools and provided the Department with timely warning of collection problems. The schools receiving indepth help under the technical assistance contract have been chosen in part on the basis of information from the quarterly reports.

As soon as final health professions student loan regulations are issued, the Department will revise the student financial aid guidelines incorporating many of the changes suggested to date for improving debt collection under the loan program.

In fiscal year 1984, the Department will conduct a series of 2- or 3-day workshops in 10 or 12 locations around the country to inform school officials on recommended or required practices and procedures. We expect that about 1,500 to 2,000 financial aid officers and others will participate in these workshops.

We have already seen a significant improvement in loan delinquency rates among participating health professions schools. At the end of June 1981, for example, almost 15,600 borrowers were delinquent 91 days or more in payments due on their loans.

This represented 11.8 percent of all borrowers who were in repayment status or whose loans had been retired. A year later, the percentage of borrowers delinquent had been reduced to 8.7 percent. In terms of dollars loaned, the percentage delinquency rate dropped from 11.8 percent to 8.5 percent during this period—a reduction of nearly 30 percent.

At some schools, the improvements have been dramatic. Between 1981 and 1982, one northeastern school was able to bring about a drop in the delinquent dollar rate from 31.3 percent to 10.5 percent.

One southern school succeeded in reducing its delinquency rate from 29.4 to 9.7 percent. At one midwestern school, there was an improve-

ment from 41.5 to 21.1 percent. A number of other schools showed a drop of one-half or more in the number of delinquent dollars.

If we limit consideration to loans in repayment status, delinquency rates for both borrowers and dollars also show improvements since 1981. At the time of your subcommittee's earlier hearings on the subject of health professions student loans in December 1981, it was estimated that about 30 percent of health professions and nursing student loan borrowers in repayment status were in default; the rate for health professions only was about 15 percent. As of June 1982, the comparable health professions rate is 11.7 percent.

Progress has also been made in efforts to reduce the delinquency rate among health professions student loan borrowers who are employees of this Department and other agencies of the Federal Government.

At the time we testified before your subcommittee last July, there were 14 remaining delinquent Department employees, out of 80 originally identified by the Office of the Inspector General.

Earlier this year, another 20 such individuals were identified by the Inspector General. Today there are only 12 out of the total of 100 identified health professionals who are still delinquent and still employed by the Department.

More recently, the Office of the Inspector General has provided the names of some 460 additional delinquent health professions student loan borrowers who are employed by other Federal Departments or agencies, including the Department of Defense, the Coast Guard, the Tennessee Valley Authority, and the Office of Personnel Management. Over the next several months, we will be verifying whether these individuals are still delinquent in their payments. Information on those who are still delinquent will be sent to the appropriate agencies for follow-up action.

You will recall that the various penalties applicable under the Debt Collection Act of 1982 to persons who owe debts to the Federal Government are not applicable to borrowers under the health professions student loan program. That is because health professionals' debts are owed to their school loan funds, not the Federal Government.

Therefore, delinquent HPSL borrowers are not subject to the provisions of the new act allowing Federal employees' salaries to be offset for repayment of delinquent debts or allowing Federal agencies to collect claims by means of administrative offset, that is, withholding money otherwise payable to the individual by the Federal Government.

Similarly, the new act's requirements for interest and penalty charges and its provisions relating to the release of taxpayer mailing addresses for the purpose of collecting debts to the Federal Government do not apply to HPSL borrowers.

The Department has proposed three legislative amendments to assist health professions schools in making further improvement in debt management. Two of these amendments are found in the administration's proposed Health Amendments of 1983, introduced by Senator Hatch as S. 963.

Section 306 of that bill would increase the maximum penalty charges a health professions school may impose for overdue HPSL

loan repayments. The current penalty is inadequate to provide an incentive for borrowers to pay promptly.

Section 307 would permit a loan in default under the health professions student loan program to be referred by the school to the Department for assistance in collecting. Before referring a loan, the school would be required to have exercised all due diligence in attempting to collect the loan.

The third amendment, submitted in a separate administration bill, would permit the Department and lenders to obtain from tax records the addresses of individuals who have defaulted on health professions schools' loans. Such disclosures are permitted to the Department of Education and to lenders in relation to schools' loans under the comparable national direct student loan program under the jurisdiction of that Department.

In closing, I would like to express appreciation to you, Mr. Chairman, and to the members of the subcommittee for your efforts in behalf of improved debt management in programs such as the health professions student loan program.

Effective debt collection is particularly important to a program that relies so heavily on loan repayments as a source of funds for new loans.

If the HPSL loan delinquency rate had remained the same at the end of June 1982 as it had been at the end of June 1981, an estimated $8 million less in loan repayments would be available over the years for new loans to health professions students.

At the current average borrowing of about $2,200 per student, this represents low-cost long-term loan aid to approximately 3,600 students in need of assistance to complete their education.

We look forward to continuing to work cooperatively with you and your staff.

Senator PERCY. Thank you, Mr. Kelso.

We have only one question, due to the shortness of time.

Last summer, I chaired a hearing in which you discussed the fact that 80 health professions student loan recipients who were employed by the Federal Government were delinquent on their loans.

Do you know what the status of those particular loans is today?

Mr. KELSO. Yes; out of the 80 that were originally referred to us, 9 of those individuals are no longer with the Department.

The remaining 71 have established loan repayment schedules and are current with their loans.

Senator PERCY. Very good indeed.

Senator D'AMATO. Mr. Chairman, I am gratified to hear these kinds of examples. It does pay off to the American taxpayer. So I think your remarks, Mr. Kelso, give us increased reason to go forward, and I congratulate you.

Mr. KELSO. Thank you, very much.

Senator PERCY. We thank you, very much indeed for being with us.

Our next witness is Robert Webber, General Counsel, Small Business Administration, accompanied by Earl Chambers, debt collection official, Small Business Administration.

We welcome both of you to our hearing today.

Small business does form the backbone of our economy.

When small businesses are prospering, our economy prospers. This is why what you are doing is so important. By collecting previous loans, you are providing money for new small businesses that need capital. In turn, this creates jobs, innovation in the marketplace, and, in general, a boost to our economy.

I look forward to your testimony.

I wonder if each witness today could start limiting their statements to 3 minutes.

The House has a 1-minute rule. You would be surprised how much they can say in 1 minute.

We have your testimony. We have studied it. Please summarize what the essence of it is.

Then we will go on to questions.

TESTIMONY OF ROBERT B. WEBBER, GENERAL COUNSEL, SMALL BUSINESS ADMINISTRATION, ACCOMPANIED BY EARL CHAMBERS, DEBT COLLECTION OFFICIAL, SMALL BUSINESS ADMINISTRATION

Mr. WEBBER. Good morning, Mr. Chairman and Senator D'Amato.

We are very proud of our accomplishments at the Small Business Administration in the area of debt collection. Our Administrator, Jim Sanders, has made debt collection a top priority. We have frequent meetings of a Debt Collection Committee. This committee is headed by our Deputy Administrator, our Comptroller, myself, the head of our financial assistance programs, the Associate Deputy, and Mr. Chambers. We have done many things in the agency to lend emphasis to debt collection. I would like to give you an idea of what we are doing.

We put 25 percent of our manpower into the servicing and liquidation of loans. Our portfolio today, as of the end of April, looks like this. We had 334,115 current accounts out of a total number of 453,000. This represents almost $17 billion in loans and guarantees that we have outstanding to small businesses and disaster victims. We have another 6,584 accounts in a deferred status. We have 21,000 accounts that are 30 to 59 days delinquent; we have 60,000 accounts that are 60 days or more delinquent, and, in the area that we are talking about today, we have 31,633 accounts or 6.96 percent of our total portfolio. What we call liquidation status.

Those 31,633 accounts, Mr. Chairman, represent $2.1 billion that we and the banks are working on to recover as much as we can for the Government. Normally, our agency recovers somewhere around 45 percent of the dollars due in that area.

In 1980, we recovered out of these liquidation accounts $139.4 million. In fiscal year 1981, we recovered $154.9 million. In fiscal year 1982, it jumped to $280.4 million, and for fiscal year 1983, we project a monthly rate of $33 to $34 million. We project total collections for this year of $404 million.

We have put emphasis not only in naming this a No. 1 priority of our agency, but have redirected staff into the debt collection work. We have increased our training. We have attempted to make our computers more efficient. We have been working closely with the Depart-

ment of Justice in providing as much support by our attorneys as we possibly can.

As a matter of fact, among our 90 field offices we have 31 specially designated assistant U.S. attorneys that handle their own cases.

We would be glad to answer any questions.

Senator PERCY. Thank you very much.

The first question will go back to the fact that you have at SBA approximately $5 billion in defaults. Defaults have increased from $480 million to $720 million in 1982. SBA therefore has 10 times as many defaulted loans in the Justice Department as any other Government agency, a total of $574 million.

How much of the $4.8 billion, or roughly $5 billion, in defaults is collectible, as a rough guess, in your judgment?

Mr. WEBBER. As I mentioned earlier, we had 31,000 accounts in liquidation. About one account out of three goes into litigation. We have now approximately 4,500 accounts at the Department of Justice. About 55 percent of our litigation accounts are bankruptices. The rest of them will be suits for foreclosure on real property and suits for deficiency against obligors. Our estimate is that we will recover approximately 45 percent of the amount owed.

Senator PERCY. Of the over half billion dollars in defaults that you have at the Department of Justice, how long have those cases been there?

Mr. WEBBER. I will tell you how we do it with our attorneys. It is rather interesting. We have a goal that is set for each attorney handling litigation cases and working with the Department of Justice. We expect that an attorney with a portfolio, say of 100 cases, to be able to turn those cases over in 15 months. Prior to the recent recession and high interest rates, we were able to actually turn those cases over in 11½ months. Today, it is getting closer to 13 to 14 months because of the numbers of cases. But we have not lost the ability to handle those cases. We will get to every one of them.

Every case is tracked.

Senator PERCY. There seems to be some discrepancy. Justice says it has only $231 million in cases. That is $240 million less than you thought they had. What happened?

Mr. WEBBER. Our computer addresses the litigation category at the time it comes to the SBA attorney. So there is in the referral process the time taken to get to Justice. I would place greater reliance on our system because we make a number of direct referrals to U.S. attorneys that are not reflected back at the headquarters of the Department of Justice.

Senator PERCY. Let's say we are talking about $574 million. That is not chickenfeed. How much of that do you think is collectable—in your judgment and your experience—and do you think that the Justice Department is doing everything they can to collect on these defaults?

Mr. WEBBER. Our historic recovery rate is, as I indicated, approximately 45 percent that will be collected. I believe our agency has had a very good relationship with the Department of Justice. I think the Department of Justice has stayed on top of our cases basically for two reasons. First, our cases are generally in large amounts. Second, we have a staff that monitors our litigation and provides support to the

assistant U.S. attorneys, some actually handling the cases. So I think that our relationships that we have built over the years with the local offices of the U.S. attorneys is something that is very helpful to us.

Senator PERCY. Legislation that we adopted previously provided for the hiring of outside collection agencies. With a default increase of a quarter billion dollars last year, and the backlog that you have of uncollected debts which rivals all other agencies—that level being $4.7 billion—why is it that the SBA has failed to use what any other business would use, an outside collection agency, if they can't get their money?

Mr. WEBBER. First, let me mention that the $4.7 billion are not accounts in liquidation. The accounts in liquidation are $2.1 billion. I think the figure that you must have there reflects total accounts in delinquent status, but will probably be brought current. Those are accounts that we have not given up on. So the collectable accounts—the debts collectable—are actually $2.1 billion.

As for outside collection agencies, we have been discussing that with different agencies. I would like Mr. Chambers to respond and tell you how our negotiations have gone to date.

Mr. CHAMBERS. With regard to contracting out internally, Senator, we have looked at slices of our portfolio. For example, 200,000 are disaster home loans all over the country, and another 70,000 are farm loans that are paid once a year. We have looked at contracting-out to attempt to see if a private company did this, could they do it more effectively than we, particularly in the disaster home loan area. If you look at all of these loans, about 75 percent of them pay exactly as they should. We estimate that it costs up 3 cents to collect $1. We have been to two companies that know how to do this. For example, a company which collects loans for credit unions estimates that it would cost them 6 cents to collect $1. Because these loans are so spread out and we do have computer terminals in every office hooked up to our main computer to track them, and are a class of loans which owe about $50 a month, we think we could collect them more efficiently than anyone else. We are not opposed to it, but in fact are looking for ways to contract out. I would like to make one point here. In the delinquencies listed here on this chart, $2.5 billion, about $400 million of them are deferred farm loans. That is a credit decision that we and the Farmers Home Administration have looked at and said, "Let's defer a payment until next year to let the commodity markets get straight, let the President's PIK program work, and to get a lot of things straight." So although there is $400 million in the total loan balance that looks delinquent, we anticipate that by next January those farmers will pay the one payment they are behind, as well as next year's payment. $400 million will then simply be moved back over to the current loan column. The farm loans are a general category we did not know much about when we got into farm lending but they are an excellent segment of the portfolio.

Senator PERCY. Thank you very much. I have one final question.

Could you give the committee an idea as to how long it takes the Justice Department to litigate the cases on average?

Mr. WEBBER. You have to divide that into the three kinds of cases as I mentioned earlier. The bankruptcy cases cannot really be con-

trolled by the Department of Justice. The case in bankruptcy has to go its course. The average time of a bankruptcy case is 8 or 9 months at least. On the other cases, as I indicated, we are running about 13 months in turning those cases over. But during that time, part of that period is taken up by the agency's referral and the preparation of the case.

Senator PERCY. I would like very much to have you take back to the SBA the thought that—in my own judgment—the debt collection process at the SBA is just too slow, and see what can be done. I would appreciate your comments in the form of a letter indicating what steps are being taken to speed up the process. We would like to give you the gold star. I will do so promptly if we see that the process is somewhat speeded up. I just think the whole thing can be moved along a little faster.

Mr. WEBBER. We will be happy to furnish a letter.

[The letter referred to follows:]

U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

AUG - 5 1983

Honorable Charles H. Percy
Chairman, Subcommittee on Energy, Nuclear
Proliferation and Government Processes
Committee on Governmental Affairs
United States Senate
Washington, D. C. 20510

Dear Mr. Chairman:

This letter is in response to your request during the hearing on May 25, 1983, that I more fully describe this Agency's progress in debt collection.

In order to describe the progress and accomplishments of the past two years, I must first describe, in an abbreviated manner, the "debt collection system" which has been developed by this Agency over the past twenty-five years. The components of that system are similar to those used by the main office of a large bank to conduct operations throughout a multitude of branches across the Nation.

The Office of the Associate Administrator for Finance and Investment (AA/F&I) establishes rules, regulations and policy for loan and guarantee programs and other financial programs such as Small Business Investment Companies, surety bond guarantees and pollution control municipal bond guarantees. An equally important function is to establish Standard Operating Procedures (SOPs) for the servicing, collection, and liquidation of the financial assistance obligations of the Agency. Ultimately, our field offices utilize these SOPs as part of their daily operations.

Supporting these activities is the Office of General Counsel whose many responsibilities include close liaison with the Civil Division of the Department of Justice, and the United States Attorney's Office on all pending litigation. It also provides technical direction to field office attorneys in much the same manner as described above for the Office of the AA/F&I.

The Office of the Comptroller establishes rules and procedures for loan accounting, accounting and control of disbursements and receipt of money, control procedures for the cashier in each office, and prepares all official reports to the Treasury and OMB. In addition, the Comptroller's Office directs the central billing and receiving functions in Denver, Colorado. A small staff, utilizing equipment linked to the Central Office computer, bills on a monthly basis approximately 300,000 borrowers in a manner similar to major credit card operations in the commercial banking world.

Before noon each day, over 12,500 checks, representing loan payments from SBA borrowers, are processed and deposited to the Denver branch of the Federal Reserve.

The Office of Computer Science is responsible for the operation and control of a Sperry-Univac 1100/81 computer located in the Washington, D.C., headquarters building. This computer is electronically interfaced with a "network" of terminals in every field office which gives all offices immediate access to an ever widening mass of loan accounting details. This "network" also provides a means of transmitting high priority messages or instructions to and from any or all offices simultaneously.

About one fifth of the Agency's personnel (850 employees) are assigned to Portfolio Management (PM), which is part of the Office of the AA/F&I. These employees are located in the Central Office and the various SBA field offices. It is their job to service, collect, and liquidate a very large portfolio of loans. This portfolio includes approximately 92,000 SBA guaranteed bank loans representing nearly 10,000 banks and $7.8 billion in contingent liabilities. It also includes: 190,000 loans to home owners and renters adversely affected by floods, tornadoes, earthquakes and other natural disasters, 46,000 disaster business loans, 68,000 disaster farm loans, and 50,000 business loans to minorities, women, and local development companies, as well as those related to occupational safety and health, coal mine safety, air pollution, water pollution, and military base closings. SBA, as a lender "of last resort", and involved in the disaster assistance program, has at times made and guaranteed loans to individuals and borrowers which were marginal from the outset.

The concept of "Debt Collection" has taken on a very significant role in government, as evidenced by your hearing. For the first time ever, collecting what is owed to SBA has been given the highest priority.

What has SBA done in the past two years to improve debt collection?

Recognizing that SBA's organizational structure and debt collection systems were already operating at a sophisticated level in the spring of 1981, we adopted a Debt Collection Plan which addressed: (1) reallocation of human resources, (2) improvement of computer and communications equipment, and (3) enhanced training.

The Office of Management and Budget assigned SBA a goal to increase collections by $100 million over the $1.285 billion collected in FY/1981. Under the leadership of Administrator Sanders, that challenge was met. In FY 1982 SBA increased its collections by $115 million.

In the reallocation of people we managed to retain, and to some degree, add positions to the PM staffs at a time of personnel reductions across the board. With the consent of both Small Business Committees and OMB, appropriations for Disaster Assistance programs were made available so that SBA could hire 275 temporary employees. By January, 1982 these employees were hired and assigned to field offices to augment collection work related exclusively to approximately 300,000 disaster loans. It is important to point out that over a quarter of a million disaster loans were added to our normal portfolio of business loans between 1976 and 1981 without an increase in personnel resources to handle the servicing activities related thereto. To further assist in the litigation effort, we initiated a program to increase the numbers of SBA attorneys designated by the Department of Justice as Special U. S. Attorneys. This designation permits our attorneys to handle their claims cases throughout the course of the litigation. In September, 1981, we had twelve such designations. We now have thirty-five and this number is constantly increasing. While each of our field offices has at least one attorney, with large metropolitan offices having three or four, the authority to use the Justice Department letterhead and to perform much of the litigation work ourselves has significantly improved turn-around times and backlogs in the Federal Courts.

The collections from our liquidation activities as tracked by our computer, indicate significant results. In FY 1981, completed liquidation cases resulted in the recovery of $155.9 million. In FY 1982, when "Debt Collection" efforts began to take hold throughout the Agency, the figure rose to $280.4 million. At the current rate of collections, this year, that figure will exceed $404 million.

An example of SBA's success in debt collection is the "Columbus Collection Plan". (See exhibit). The plan required the Agency to pursue a group of borrowers whose loan balances had been charged off. Working with the Department of Justice and the media, the Plan was implemented and the results were immediate. The success of this plan has spurred agencywide distribution so that the Plan can be implemented across the Nation.

In the computer/communications portion of our Debt Collection Plan, the changes brought about, and those which are imminent, are also noteworthy. Because of Executive and Congressional emphasis, internal decisions as to expenditures on computer and other electronic equipment improvements quickly fell in place. Our conversion to a new data based system was accelerated. Updating of the automated loan accounting system has been improved by a factor of five. The time between receipt of payments in Denver (deposited before noon to the Federal Reserve Branch the same day as received) and the electronic transfer of that information to our Washington

data base now takes only a few hours instead of days. Using this system any office can have access to the Univac and determine whether or not a given borrower made payment the previous day.

A very important aspect of this system is savings in postage. Instead of boxes of computer reports being shipped to every SBA office once a month, timely and accurate data is now electronically transmitted to high speed printers in each office. If the office needs the details of a given loan, it can get a display or printout in seconds. We are also currently redesigning management reports to ensure that pertinent and useful information is gathered. Not only do collectors and loan servicing officers have access to the very best collection information available, but managers and supervisors are beginning to be brought into this electronic loop at an ever increasing rate. Our strategic goal, to use a phrase from the best selling book Megatrends, is to develop a paperless collection system. Of course, the obvious result of a truly automated system which does incalculable amounts of work in seconds means that SBA can do more, and more effective, collection work with fewer people.

The third element of our Debt Collection Plan efforts is, and has been, to provide staff training. Training budgets are directed to four different segments. The first is our 250 liquidators who deal exclusively with the most serious collection cases. We were determined to improve our "recovery rate" of the $2 billion in liquidation from the 48.4 percent statistic of FY/1981. During the winter and early spring of FY/1982, our Portfolio Management staff from Washington conducted five training sessions for all of our liquidators and many of our attorneys. This helped to improve our recovery rate so that as of April, 1983, it stood at 65.9 percent. The cost of this training was about $150,000 but the benefits to the taxpayers was in the millions of dollars.

The second segment to receive directional training was the group of Portfolio Management (PM) chiefs. In each district office the PM chief must manage servicing, collections, liquidations, reports, goals, etc. for his or her office. Again, the Central Office staff of Portfolio Management set up and conducted five sessions of three days each to orient and redirect debt collection objectives. These sessions were held in the late spring, mid-summer, and early fall of 1982.

The current PM training series is now three fourths complete with the last session to occur in St. Louis in September. These four sessions of approximately 60 people at each are directed at mid-level employees in PM offices. This training is supervised and largely conducted by Washington based PM staff. It includes key senior level supervisors from the Comptroller's Office, the Office

of Computer Science, and from the Administrator's staff. The attendees are the people who do the kinds of work banks routinely do with their loan customers, and which is also performed by collection agencies. They respond to "customer" requests. They make collection calls. They operate the equipment. They prepare the reports. They are the backbone of the organization. These training sessions were designed to fully orient these key people with the teamwork efforts from many sources that are being coordinated for their use in debt collection. The sessions last two and a half days and are immediately followed by a full day of training for which we contracted with Dun & Bradstreet on the topic of telephone collection techniques.

Finally, we have emphasized debt collection in our attorney conferences. At the regional counsel's conference last September in Leesburg and at a similar one this past April in Boston, great priority was given to debt collection and the increased concentration of SBA attorney resources on claims litigation and related collection activity. This was also true with respect to the Eastern and Western regional conferences held in Williamsburg, Virginia, and San Diego, California, respectively. These conferences which involved most of the Agency's attorneys also provided increased substantive legal training with respect to debt collection and claims litigation.

Two of the Administrator's four Agency priorities are aimed at reducing our losses on loans. One is to improve debt collection. The other is to make quality loans. The new focus on quality loan making now has a more sensible and realistic meaning for small businesses, for banks, and for the taxpayers of this country. Quality lending goes hand-in-hand with quality debt collection. A good credit institution needs both. We have both and both are improving.

I appreciate the opportunity to describe our programs in debt collection. If you should need any additonal information, we will be pleased to respond.

Sincerely,

Robert B. Webber
General Counsel

Senator PERCY. Senator D'Amato.

Senator D'AMATO. Mr. Chairman, I think that in your usual way, you are so very gracious. I would suggest that there has been a lack of the kind of activity necessary to carry out the guidelines set by OMB.

I refer specifically to the GAO report, "Although SBA developed the debt collection plans for fiscal 1982 this plan does not meet OMB requirements and cannot be clearly linked to significant improvements."

Further down it addresses specific problems or issues confronting the agency's debt collection activities. "In general they did not set out specific deadlines." It goes on to say, "SBA resisted much of OMB's guidance."

I want to tell you, I think the chairman is very, very gracious. I am not. [Laughter.] I am not. No, I am not. I will fight for you fellows. And I do. As a member of the Small Business Committee, I fight to give you expanded authority, to get the kind of funding which is necessary. I will continue to fight for that so that you can do your job. But doggone it, we have an obligation to see to it that it doesn't take 13 months to forward the case over from SBA to Justice. You don't have the computer capacity and the Justice Department doesn't have the computer capacity. You want to start playing games over here and say nice, nice, Justice Department.

I know that. I know the game. Don't come here before this committee saying we are making significant improvements because you are not. I would flunk you. But you had better start making significant improvements. I think the chairman has been just so terribly patient. But he has several years on me. I guess you learn that after time. But I just don't think, Mr. Webber, that you are doing the kind of thing that OMB is calling for and that the law is calling for. What happens is that this jeopardizes the Small Business Administration and its programs. The demagoguery will occur. Some will say $4.7 billion we are not collecting. There are a lot of people out there, working middle class families, who say, that is right, the heck with that program.

If that is what you want to take place, you just continue that. You are going to make it a lot easier for people to stop funding programs and they are going to start cutting back on them. If you want to enhance SBA, you go ahead and pursue debt collection with some diligence.

Thank you, Mr. Chairman.

Senator PERCY. Thank you, Senator D'Amato, for your restrained comments. [Laughter.]

I think probably the greatest tragedy is we don't have a really tough policy and have not developed a reputation for being a tough business enterprise. It not only jeopardizes your ability to continue loans in the future, but what it does is cause a flood of applications and people who give all the bureaucrats a lot of paperwork, but who don't want to go to the commercial bank because they know those guys mean business. They want their money back. They are going to flood you with applications when they could go, maybe some would qualify, could find a way at a commercial bank. But if they don't have to pay you back, why should they pay, why should they deal with a bunch of guys who want it back. It is the same as student loans.

Small business people get that feeling, also. It is in the national interest to help business. I think it is a matter of discipline that we are really both talking about here. I would like to hear from you as to what steps are to be taken to speed up the process.

Mr. WEBBER. May I say, Mr. Chairman, in response to your concern and Senator D'Amato's, the Administrator and the people in our agency feel we are making progress. We think we have shown figures here that are greater than the year before that show improvement. We are doing our best and we will get back to you in a letter. We will do everything we can to work with OMB and meet their guidelines.

Senator PERCY. Very good. We thank you very kindly for your presence today.

[Mr. Webber's prepared statement follows:]

SBA U.S. Small Business Administration Washington, DC 20416

CLASS Document
File 6-E(2)

STATEMENT OF ROBERT B. WEBBER
GENERAL COUNSEL
SMALL BUSINESS ADMINISTRATION
BEFORE THE

SUBCOMMITTEE ON ENERGY, NUCLEAR PROLIFERATION AND
GOVERNMENT PROCESSES
COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

May 25, 1983

MR. CHAIRMAN AND MEMBERS OF THIS SUBCOMMITTEE:

We appreciate the opportunity to appear before this Subcommittee. I believe that the debt collection initiatives of this Administration and your efforts with respect to debt collection are both timely and highly commendable.

As a result of the Small Business Administration's statutory loan making mandate, we currently have nearly 454,000 loans on our books. This number represents about $8.5 billion in direct Government loans and another $8 billion in guaranteed loans. This portfolio is administered by a professionally trained staff located in approximately 90 field offices.

SBA functions much like a large bank with respect to its lending programs. These programs include not only business loans, but loans to natural disaster victims, who have been devastated by floods, tornadoes and earthquakes, and to tens of thousands of farmers affected by drought and other adverse weather conditions. In addition, SBA has other statutory lending initiatives, which

address such national concerns as minority business, women in business, and those businesses harmed by the effects of Federal programs such as OSHA, pollution control, military base closings and energy shortages.

The efforts of our debt collection staff begin with loan approval and continue until the loan is either paid in full or no other avenue of collection remains. The large majority of our loans are current and require only routine oversight. If repayment problems develop, our staff can proceed to enforcement action or provide remedial relief. For instance, alternative repayment plans to resolve cash flow problems are often developed. If remedial efforts prove unsuccessful, a decision is made to enforce payment. Approximately 31,600 loans are currently in this "Liquidation" classification. Once a loan is classified as "in Liquidation" foreclosure of the collateral is first sought. We also have clearly defined procedures to compromise debts in instances where collateral has been exhausted.

Individual cases are classified as "in litigation" and referred to the Department of Justice only when court action is necessary. The referral letter has traditionally outlined previous collection efforts and present collectibility. Usually a suggested complaint accompanies the referral. Our efforts usually do not stop at this point. SBA attorneys prepare much of the pleadings and work with the various U. S. Attorneys' offices in

court. Where designated, they also serve as Special Assistant United States Attorneys and take complete responsibility for the entire litigation process. We have developed almost thirty such designations currently, and where staffing permits, intend to increase designations in the future. Moreover, SBA loan officers participate in judicial sales, and the Agency's compromise claims committees work closely with the Department of Justice to achieve the highest possible recovery.

Our collection process, therefore, provides all the necessary ingredients for collection followup. It starts with general servicing, and proceeds to problem resolution, liquidation or litigation as the situation requires. We have specialized staff personnel at each level and clear rules for them to follow.

I turn now to the specifics of our debt collection efforts. These efforts derive from the work of approximately 800 professionals in our Central and field offices whose job it is to manage the SBA loan portfolio and collect the indebtedness owed to SBA. To aid these efforts SBA has a Univac computer system in our Central Office to provide information concerning debts to SBA management. In addition, we have Burroughs billing and payment receiving equipment in Denver which is used to receive payments. It puts about $5 million into the Denver Federal Reserve Branch Bank every business day of the year. Every SBA office also has at

least one CRT and keyboard system, which contains a high speed printer to receive and send information back and forth to the Univac.

There is at least one SBA attorney in every field office to handle the lawsuits and judicial foreclosures in connection with the Department of Justice. As previously mentioned, some SBA attorneys serve as Special Assistant U. S. Attorneys for debt collection purposes. We began FY 1982 with 11 such appointments and ended the year with 22. Over the years we have developed a cooperative and close working relationship with the Department of Justice.

Our accounting staff, too deserves credit in this effort. They keep track of the financial details of our debt collection effort, and meet deadlines for provision of data, not only to our staff, but to the Department of Treasury and the Office of Management and Budget as well.

When new Administration debt collection initiatives were announced by OMB in the Spring of 1981, SBA's plans in this area became centered on improving our already effective collection force. First, we focused on directing existing staff to this effort. This is one of the most critical factors in our present personnel management effort. In addition, it was decided that the computer systems in our main office and in Denver had to be made more efficient. Finally, we examined the training requirements for the SBA staff engaged in debt collection.

Our objective for FY 1982 was to collect $100 million more than in 1981. As a result, collections for FY 1982 totalled $1.4 billion, up from the $1.285 billion collected in FY 1981. We believe this is a remarkable achievement. To put it in some perspective, our salary and expense appropriations to operate the entire Agency with all of its programs and people for FY 1982 was about $240 million. The cost benefit of our debt collection effort when measured against this figure was almost six to one!

As you can see, we are taking debt collection very seriously. In these times of diminished personnel resources, we have attempted to maintain sufficient numbers of people devoted to our collection activities. In fact, by reallocation of personnel within SBA, we have slightly increased the present numbers involved in debt collection over past allocations. In the computer and communications field, we have spent about $1.5 million on software and programming improvements. Our conversion to a data base system is now virtually complete, and this will allow overnight updating into the central computer here in Washington of all collections deposited daily to the Federal Reserve in Denver. Each field office now has screens, consoles, and high speed printers with which collection data can be transmitted in minutes. The District Offices in Puerto Rico, Alaska and Hawaii have come in line into this system thanks to undersea cable and satellite hookups. Our efforts in this regard

during the past year make us comparable with the techniques and technology of very large banks, credit card systems, and collection companies.

We have taken steps to deal with the dramatic increase in claims litigation. That caseload has increased in the first six months of FY 1983 from 8,961 cases in October to 11,018 in April. These steps include a new standard litigation report form for claims litigation which was instituted by the Department of Justice on March 31, 1983. SBA participated in drafting the form. The form, which is now mandatory for claims referrals, requires much more detailed credit information with respect to SBA debtors, and should thus help to expedite referrals and recoveries. In addition, the form must be accompanied by draft demand letters and a complaint, which should also further expedite referrals. SBA has taken the additional step of integrating the form into its word processing equipment for use throughout the Agency.

Secondly, SBA has exercised its authority to hire an additional 150 temporary debt collection personnel to handle the increased liquidation and litigation caseload.

Finally, SBA has urged its participating banks to shoulder greater responsibility for loan liquidation and litigation. Thus, in September 1981 banks were responsible for liquidating 2,606 loans, and SBA 9,641. However, last month the banks were

responsible for the liquidation of 4,553 loans and SBA 14,434. We are taking steps to increase the banks' role even more to meet the increased caseload.

However, there is more that we can do to improve our debt collection activities. Utilization of the provisions of the Debt Collection Act of 1982 is one of the means to accomplish that improvement. We are particularly interested in making use of Sections 3 and 13 of the Act. As you know, Section 3 of the Act provides a mechanism by which SBA may disclose to a consumer reporting agency (credit bureau) its claims against an SBA borrower. This may only be done, however, after following certain procedures. Although these procedures are time consuming they are necessary, and SBA believes that Section 3 of the Act if properly implemented, will be of value in securing the cooperation of otherwise reluctant debtors.

Section 13 of the Act permits us to contract with private debt collection agencies for specified collection services. We have studied this approach to debt collection and have met with several private organizations involved in debt collection. We have also recently completed an in-depth study of our own efforts in this regard. We are attempting to assure ourselves that such contracting will be cost effective in view of our own efforts and expenditures in the debt collection area before we implement it. But, we welcome this provision as a means for debt collection.

In conclusion Mr. Chairman we are showing results in accelerating debt collection. For the past four years on accounts classified "in liquidation" the SBA shows the following recoveries: FY 1980 $139.4 million; FY 1981 $155.9 million; FY 1982 $280.4 million; and for FY 1983 we project $404.0 million.

Mr. Chairman, I will be pleased to respond to any questions you may have at this time.

Senator PERCY. Our next panel consists of Ralph Olmo, Comptroller, Department of Education, accompanied by Richard Hastings, Director of Student Financial Assistance Management, and Jack Reynolds, Coordinator, Collection Task Force, Department of Education. Joining this panel will be J. Paul McGrath, Assistant Attorney General, Civil Division, Department of Justice.

We want to welcome the panel and the witnesses to today's hearing. I want to welcome especially Mr. Olmo, and Mr. Hastings, from the Department of Education, both of whom have testified before this committee previously. I would commend Mr. Olmo on two fronts; first, for his courage in appearing before this subcommittee again. [Laughter.]

The last time Mr. Olmo was here I did give him a rather rough time. Second, for your really outstanding efforts to get started in collecting student loans. A tremendous effort has been made.

I was very critical of the Department of Education last July, because of its failure to seek repayment from delinquent Federal employees and from beneficiaries of the Cuban student loan program uncovered in a 1980 hearing. Since last July's hearings we have seen a dramatic turnaround which we will hear about today. I want to commend Mr. Olmo, Mr. Hastings, and Mr. Reynolds for a job well done. What we will hear will serve as an example of what can be done by other agencies to collect overdue debts.

But there is still work to be done. Not nearly enough of these defaulters who are able to pay, but simply don't, are not being taken to court. There is simply not enough of a feeling that there is a final recourse that we may, can and must take. We feel the ability is there, the willingness is not. I intend to get to the bottom of the problem today and get some solutions. I will ask you to make a few comments first, Mr. Olmo, and we will ask you some questions. Then we will turn to Mr. McGrath from the Department of Justice.

TESTIMONY OF RALPH OLMO, COMPTROLLER, DEPARTMENT OF EDUCATION; RICHARD HASTINGS, DIRECTOR, STUDENT FINANCIAL ASSISTANCE MANAGEMENT, DEPARTMENT OF EDUCATION; JACK REYNOLDS, COORDINATOR, COLLECTION TASK FORCE, DEPARTMENT OF EDUCATION; J. PAUL McGRATH, ASSISTANT ATTORNEY GENERAL, CIVIL DIVISION, DEPARTMENT OF JUSTICE; AND BOB FORD, DEPUTY ASSISTANT, DEPARTMENT OF JUSTICE

Mr. OLMO. Thank you, Senator Percy, and your staff, for the strong support which you have provided in passing the Debt Collection Act.

The Debt Collection Act has been instrumental to our efforts, to strengthen our credit management program. It has been very helpful to the Department as has your assistance and encouragement.

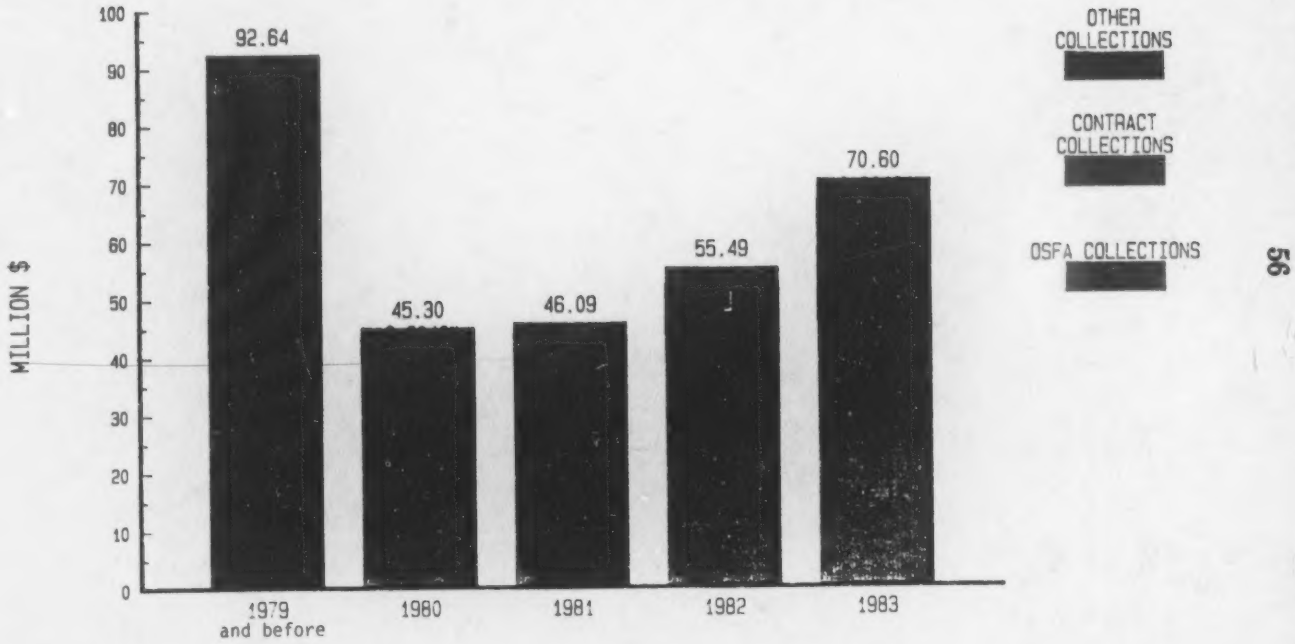
As you and Mr. Steinberg generously noted earlier, the Department has gone all out in the debt collection effort and has achieved considerable results. But we are also very aware that we have only just begun at the Education Department.

I would like in this regard, if I could, to divert from the testimony and summarize the various dimensions of the Department of Education debt collection effort.

The numbers on the chart up here on my right show the Department of Education having $10.7 billion in receivables and approximately a 30-percent delinquency rate.

[The chart referred to follows:]

PERCENTAGE OF COLLECTION DOLLARS, BY SOURCE, FY'79-FY'83



S. WEISS
MAY 11, 1983

Mr. OLMO. We have three major dimensions to the Department's student assistance debt collection program. It involves the federally insured student loan program where lender's loans are insured by the Department, guaranteed student loans where lender's loans are insured by State guarantee agencies and then reinsured by the Department. In addition, we have institutions of higher education around the country that operate the national direct school loan loan program. The Department's debt collection efforts are directed toward defaulted loans that the lenders have been unsuccessful in collecting and include in-house collecting and the use of a private collection contractor.

Of the $10 billion or so in the Department's receivables, approximately $7 billion or 70 percent of that is in the area of student loans and about $4.3 billion of that $7 billion plus is in the revolving funds of the institutions of higher education around the country which are used to operate their national direct student loan program.

One reason I wanted to summarize the Department of Education's portfolio is to show that the percentage of receivables that are delinquent in the Department is not a useful measure in the case of student financial aid because we don't have loan collections in our portfolio unless they are delinquent. Thus 100 percent of the student loans in the Department of Education's portfolio are already delinquent when they are received for collection.

As we wind down some of the programs that generate other receivables, such as our housing and facilities loans program, amounting to about $3 billion, and if we are successful in the administration's proposal to reduce the level of the revolving fund in the national direct student loan program, the percentage of delinquencies in the Department's portfolio will increase.

Presumably some time in the future, 100 percent of the loans in the Department of Education will be delinquencies. That is important to note. A more appropriate measure for the Department's progress in this area would be to determine the level of collections relative to the level of receivables in the portfolio. That is how we attempt to measure progress in the Department in terms of its delinquent collections situation.

An important part of our challenge is to prevent accounts from going into default by setting standards and providing incentives to our parters in the process. That is the lenders, the guarantee agencies, the higher education institutions as well as the borrowers.

Just over the last 3 years, some $21 billion have been lent out nationwide in the guaranteed student loan program alone. Those kids are still in school. We haven't yet determined nor felt their social impact.

We, of course, know a certain percentage of those loans will go into default, and will be submitted for reinsurance payment. We have got to prepare for that. We are working with all of our partners in the process in order to make the appropriate and necessary preparations.

I appreciate the opportunity to provide that explanation of the nature of our portfolio. It is so different that I wanted to summarize it and why it is important to note that the delinquency rate in the Department can be misleading. It almost assuredly will increase in spite of a dramatic improvement that we make in the debt collection effort.

We are moving rapidly to implement the provision of the Debt Collection Act and would like to outline steps that we have taken to exercise the authorities contained in the following three key provisions of that legislation.

First, the Debt Collection Act provides authority to refer delinquent borrowers to credit bureaus and to implement this procedure we have established systems necessary to carry it out. By the end of the year we will have referred some 500,000 borrowers with defaulted accounts to credit bureaus.

Second, the Debt Collection Act authorizes salary offset against Federal employees who are defaulted on student loan repayments. To implement this procedure we have already sent out notices to defaulters who are Federal employees.

We have some $67 million in loans identified with 46,860 Federal employees. We have already received collections of $2.3 million just from the initial letters. Secretary Bell has taken a great personal interest in this process. We met with him this morning.

He is about to brief the President's Cabinet in the near future to activate the administration's overall strategy for the off-set recovery process.

Third, the act authorizes contracting with private sector collection services. I believe there is a schedule passed out to the members of the committee which showed indeed as you mentioned earlier, Senator Percy, that virtually all of the increase in the Department's collection effort from 1982 to 1983 was a result of the contract.

Last, I would just tell you that we are very concerned, of course, about the litigation issue and let you go ahead and ask questions if that is all right.

Senator PERCY. Thank you.

We will do that. I will start with Mr. Hastings.

One of the most serious questions we faced when we got into writing this legislation was how to handle the problem of finding people. I was shocked to discover the Federal Government doesn't ask for social security numbers.

I wonder if you could recount the experiences you have had, Mr. Hastings, after you have referred cases to the Justice Department and they have advised you they could not find the people. What has been your own experience in trying to go after and find the debtors?

Mr. HASTINGS. The joint standards, as I recall, require that the addresses we provide be current within the last 6 months, I believe, when we refer a case to Justice.

We have tried to be very diligent in following that standard.

At the request of the staff, we did pull at random five cases in each of our three regional offices which are involved in collections. We followed up on those. None of these accounts have been collected as I recall. I believe one or two of them may have a judgment. But I don't believe we received any money on any of them.

In several cases, we were informed by the U.S. Attorneys' offices that they were unable to locate the debtor. In our Chicago office yesterday we found within 3 hours four of the five cases that came back to us.

Two of those people, I believe are in the phone book. I am also advised that some of these debtors are at the same address that we gave the Department of Justice, in some cases as early as 1979.

They have not moved from that address.

Senator PERCY. Again, going back to previous experience, it is just so unconscionable to think we really don't use our best efforts in all of the services that we have to find people.

As I go through individually, as I have in each of these cases where Justice has indicated they couldn't find the people, even cases where they have found the person, finally after a year's research they found the person and nothing has been done since then.

Getting back to May 1982, the effort was made to find them. They finally did find them. Nothing was done.

Here is another case, $5,527 owed, out in Detroit. It goes back to September of 1979 and U.S. Attorney has told OSFA, "Sorry, but we have not had a chance to work that one."

So we have a real problem here of backlog and jam up that is hindering our projects.

Mr. Reynolds, it is important that we in the Congress understand how far behind the Justice Department is in taking these defaulters to court. How many cases have you sent the Justice Department for litigation and how much money is involved?

Mr. REYNOLDS. According to records, it indicates that Justice now has the responsibility for approximately 22,000 of our cases that are valued at around $48 million. Justice disputes those figures.

Senator PERCY. How much?

Mr. REYNOLDS. $48 million.

Senator PERCY. Is that the total debt that they are going after?

Mr. REYNOLDS. Yes; that would be the principal, the accrued interest at the time we turned it over, and any interest that has accrued since that time.

Senator PERCY. Can you tell me of the total amount of debt involved in that particular block of bad loans how much have they actually collected?

Mr. REYNOLDS. Our records show approximately $7 million.

Senator PERCY. About $7 million?

Mr. REYNOLDS. Yes.

Senator PERCY. I understand the Department of Education has very little confidence that the cases that they send to Justice will be promptly litigated.

Is that true? If so, why?

Mr. REYNOLDS. Our major concern, sir, is the timeliness of litigation. As Mr. Hastings indicated, the Joint Standards require that we have a recently verified home address—current within the last 6 months.

Our contention is that the cases sit, at the U.S. attorney's offices in a lot of cases and, therefore, the borrower has moved by the time they get around to the actual litigation of the case.

That is our major concern.

Senator PERCY. How long has the Justice Department had these cases?

Mr. REYNOLDS. Of the 15 we surveyed yesterday, they have all been with Justice since 1979. The majority of the turnover of our accounts

to Justice occurred in 1979 and 1980. That would be the majority of those 22,000 accounts.

Mr. HASTINGS. If I might comment on that question, Senator Percy, one of the problems we have, and really why we have been so concerned about this issue recently, is because of our use of private collection agencies.

As Mr. Olmo's testimony indicated, because of the Fair Debt Collection Practices Act, there are restrictions on what the collector can say on the telephone if he doesn't have the ability to make it occur.

We are in an awkward position with the use of our collection agencies because they cannot say this account is going to be sued if nobody is going to follow up on that. They place themselves in jeopardy in that case.

Second, these agencies are working on a contingency basis. They have invested time, effort, and dollars, obviously, in skip tracing many of these accounts. They have located the debtor. The have the information that is necessary for litigation. They don't get anything out of the process if nobody is going to follow through to litigate the case.

Senator PERCY. Are you holding back large numbers of default cases from the Justice Department because you fear cases will just sit?

Mr. HASTINGS. We did a survey a couple of weeks ago, I guess, in large metropolitan areas of the United States. I believe we have identified about 26,000 cases which do meet the criteria for litigation and which should be turned over to the Department of Justice for litigation.

There is a great deal of manual effort involved in the preparation of those cases and we have been discussing some experiments to reduce a lot of that paperwork.

Senator PERCY. So the potential is really quite great?

Mr. HASTINGS. Absolutely.

Senator PERCY. Mr. Hastings, one of the most outrageous debt collection problems we uncovered was the finding that so many of the Government's own employees have refused to repay student loans.

Last July, this subcommittee found that little or no action had been taken against Federal employees in default. In fact, the Department of Education had destroyed or lost the list of employees in default.

Within 5 months of that hearing, this situation was turned around. By December, Education had sent 46,000 letters to federally employed defaulters demanding payment and making it clear that those not complying would have their wages offset.

I want to commend the Department very much, indeed, for the work that has been done.

How much has the Department collected since these letters were sent out?

Mr. HASTINGS. I believe the testimony indicated about $2 million.

Mr. OLMO. $2.3 million has been collected up to this point and some 1,300 of the students have paid off this in full.

Senator PERCY. How much do you have committed as a result of that, in addition to the actual $2.3 million that you have received?

Mr. OLMO. Mr. Hastings has that information.

Mr. HASTINGS. About $7 million is the value of the accounts in repayment.

Senator PERCY. Tremendous. What are costs to the Government to send out the letters that were dispatched to employees?

Mr. HASTINGS. I would estimate around $50,000.

Senator PERCY. That would bring about $40 minimum return on investment just on dollars received and probably over $100 based on expectations that you have now.

What was the largest payment that you received?

Mr. HASTINGS. The largest one, interestingly, happens to be one that was collected by one of our collection agencies, for about $12,000. It was a husband and wife, both of whom are doctors, both of whom were employed by a branch of one of the military services and both of whom were in default. They are paid in full.

Senator PERCY. How many salaries of Federal employees have you set off to collect the debts as promised in the letter? We have for the first time authority to offset salaries under the provisions of the Debt Collection Act of 1982.

Mr. HASTINGS. We have made no offsets yet under that authority.

Senator PERCY. So you have had that as an ultimate weapon, but you haven't felt it necessary to use it yet? I agree with you. You are getting a greater return. It is good. However, it will have to be implemented just as my farmers from Illinois told me today. They are involved in the Farm Credit loans. They have got to ultimately have a foreclosure. They have got to realize the pressure comes down. These are not gifts. They are loans. They have got to be repaid to the very best of their ability.

It is not unlike IRS. It seems that 20 days or 30 days before we file our returns, there is always a prominent case on the front page of the paper. Someone has gone to jail, or a suit is filed against them for failing to pay their tax. It helps make millions of people a little more honest with that pencil than they would have been otherwise.

Mr. OLMO. Excuse me, Senator, we expect we will undoubtedly have to use the offset provision in a number of those defaulted loans of Federal employees. We are moving along in the process. As I mentioned in the testimony, Secretary Bell will be briefing the other Cabinet members very shortly in order to implement those offset procedures. In addition we have the regulations that have been, still need to be finalized before we can finally effect the offset. We will have a 60-day period that the individual agencies will be provided notice to the employees within their own agencies.

We published those regulations yesterday.

Senator PERCY. So, now that they are published do you feel you can get on with the program?

Mr. OLMO. Yes. There is a 60-day review period.

Senator PERCY. Senator D'Amato?

Senator D'AMATO. Mr. Chairman, I think that the Department of Education and Secretary Bell and Mr. Olmo, Mr. Hastings, and the entire staff, Jack Reynolds, Stuart Weiss, they have been most cooperative and helpful in giving us the kind of insight necessary to develop a legislative approach which will make the job an easier one. I just want to commend you. You have been pressing forward and have made just incredible strides. Mr. Chairman, if we can get some other agencies or departments to move with this kind of determination

23-137 0 - 83 - 3

and purposefulness, why, we would go a long way toward rectifying one of the great problems which has occurred over these years. That is taking a loan program and having people believe it is nothing more than a giant program because no one is going to come after you, no one is going to make a reasonable effort to collect the loan. So I want to bring forth that throught. You've done a fine job. We recognize, however, there is more to be done.

There has been a heck of a turnaround in these past several months.

Senator PERCY. Thank you very much indeed. There has been. I second everything that you have said.

Mr. McGrath, we welcome you today. Is Mr. Ford with you, by the way?

Mr. MCGRATH. Mr. Ford was here before. I don't know whether he is here now. He would not be appearing.

Senator PERCY. Is he still here? Thank you very much indeed. We appreciated your testimony in the past. We appreciate your being with us today.

I think the Justice Department does have a huge problem here. I know that you recognize it and we recognize it. Justice has not been equipped to handle the problem of defaulted loans, especially student problems. You haven't been geared up for that in the past.

Without outside help, you have little chance of collecting on more than a tiny fraction of the tens of thousands of cases now sitting over at your Department. And, over the next few years, spurred by the Debt Collection Act, other agencies may send you hundreds of thousands of cases.

No one expects you or anyone else to take all these cases to trial. The mere threat of legal action is usually enough to get a debtor to pay up. As in the private sector, 90 percent of Federal debtors who have suits filed against them never answer the complaint. Typically, they just pay what they owe.

Senator D'Amato and I have felt for some time now that you need outside help. We are pleased that you have come to agree with us. I look forward to your testimony.

Mr. MCGRATH. Thank you, Mr. Chairman. I would ask my prepared remarks be made a part of this record.

Senator PERCY. The full comments will go in the record.

Mr. MCGRATH. Thank you, sir.

I would like to briefly touch on two points. One is the status of the Department's debt collection efforts at the present time and the other is the legislative proposal that we have made which would be designed to help clear up the backlog which we now face. Until about a year and a half ago debt collection was a very low priority matter in the government generally and in the Department of Justice in particular. In the Department of Justice there was no central coordination and control and thus the job done was, necessarily, a spotty one.

I don't say that to criticize anyone. We only had a given amount of resources and when priorities are given to other matters those matters get the attention. In mid-1981, however, the determination was made to treat debt collection as a very high priority item. That was consistent with this administration's efforts to treat fraud, waste, and abuse as a very high priority item.

In that connection, the Attorney General asked me personally to coordinate our efforts on a department-wide basis, not just in the Civil Division. He made it very clear to me that debt collection was to take top billing along with others of the Department's highest priorities, such as organized crime.

With the assistance of Bob Ford, we have devised a number of concrete proposals which have moved us a long ways forward in the last 1½ years. Nobody is going to pretend we are nearly where we want to get but we have moved a long ways forward. We have done it with training, we have done it with new equipment, we have done it with new people.

In particular, we have done it with a lot of personal pressure on the U.S. attorney's offices around the country. We are proud of the results to date. In the first year for which we have overall statistics, fiscal year 1982, the U.S. attorney's offices collected about $150 million in cash for delinquent loans. For the first 6 months of 1983, that number is $83 million, which is about 23 percent over the first half of 1982.

A lot of additional things need to be done. In particular, right now we are in the process of installing new computer software programs, and new equipment, and training additional people. However, we do have one immediate problem. Over the years, as you indicated Mr. Chairman, the various departments have been allowing delinquent loans to pile up. Again I am not criticizing anybody. The departments generally were in the mode of passing out money and the problem of collecting loans was not one that people were geared up for. A principal problem we have right now is that we have been informed by the Department of Education that they have as many as 400,000 delinquent loans that have not been collected despite all efforts, including the use of outside collection agencies.

That is a large group of loans to be dealt with at once. Obviously, we expect that only a fraction of those will be referred for litigation because we know that in the process of using the private agencies, many of these loans will be found to be uncollectable and the individual debtor cannot be located in many other cases.

We could handle all of these loans but what we would have to do would be to gear up on a crash basis to handle a huge backlog and then presumably once that backlog was dealt with, we would dismantle what we had set up. We don't think that makes very much sense. What we would propose instead is that in those offices, and many of the U.S. attorney's offices will fit into this category, where the office is sufficiently geared up to handle the loans, that U.S. atttorney's office would handle the loans. However in the case, particularly of some of the larger offices, that have been more swamped than others, we think that the best solution is for the Department of Justice to be given permission to retain private counsel to assist in clearing up this backlog. We do not propose to enter into former contracts in the usual Government sense with private counsel. The legislation that we have proposed would give the Attorney General the authority to retain counsel as we do in many other situations on an individual basis without complying with the cumbersome Government procurement rules because otherwise we won't be able to get private counsel in place.

Senator PERCY. Let me just interrupt you on that particular point about the distinction between urban area and rural area U.S. attorneys. I will read from your submitted statement, "We would like to continue using our U.S. attorneys, retaining private counsel only in those categories usually in major cities where the number of debt collection cases overwhelms our resources."

We do have a problem in the major cities. There is no question about that.

Mr. MCGRATH. Absolutely.

Senator PERCY. But, how about Muskogee, Okla., Tyler, Tex., Roanoke, Va., or Cedar Rapids, Iowa? According to the U.S. attorney by U.S. attorney breakdown of the student loan default cases, all four of the cities that I have mentioned with rural U.S. attorneys have worse collection percentages than New York City, Chicago, or Los Angeles.

In fact, the U.S. attorneys in Cedar Rapids had more than twice as many default cases on their books as the U.S. attorney in New York City. In St. Thomas, in the Virgin Islands, the collection rate is only 2 percent. In the last 2 years they have collected a grand total of $105 on $23,000 in defaulted loans. Do you not agree that you need help just about everywhere, big cities, small towns, even the Virgin Islands?

Mr. MCGRATH. Senator, addressing that particular point, I do not agree that we need the kind of help that we are seeking legislation for in those areas. We are seeking legislation to provide us with assistance where our resources could only do it if they were augmented to a point where, frankly, we do not think it makes sense because we are dealing with a backlog problem. In other U.S. attorney's offices where we have problems we have been dealing with those problems. They are not backlog problems, they are current organizational problems.

I will give you an example. Tulsa, Okla., which is bigger than some of the cities that you mentioned but perhaps not all, was one of the first offices where we dealt with this problem. In that office, they got in good equipment early on and they trained some new people to do debt collection. With no more resources than were used in some of these other offices, they managed to get current—and not only current, but to have additional room in their system for debt collection cases. We have not been able to deal with all 96 U.S. attorney's offices and to get them up to the speed we would like to get them up to in the 1½ years we have been doing this.

We have, however, been able to do it in a large number of offices and we are confident that over the next few months, other offices will fall in place. The problem we have, however, is that in certain of the large offices the numbers of loans are so great that there has gotten to be a backlog and as we get tens of thousands of additional education loan cases or HUD loans, they won't be able to handle them expeditiously. In particular, I refer to Los Angeles, Chicago, and New York.

Those are the classic examples. But I don't mean to limit it to those places. Therefore what we want to do is to get the legislative authority to retain outside counsel because we are concerned that we do not have it for this particular area now. We need the authority to retain them along the lines you have suggested. Most importantly, we need the authority to pay them out of the proceeds. That is the usual manner in which the private debt collection agencies or law firms are retained.

We are very concerned that under such laws as the Anti-Deficiency Act we do not have that authority right now. I think there is general agreement on that.

Therefore, we have proposed legislative language which would permit us to employ outside counsel. If we are given that statutory authority we do intend to do it. Under our regulations, the authority in this area is delegated to me. I do personally intend to move on this immediately if we are given that statutory authority.

That really touches on the major points that I wished to make. I would be happy to try to answer any questions of the committee.

Senator PERCY. Very good.

In your statement you have indicated that U.S. attorneys could collect each dollar for a mere 6 percent as compared with commercial litigation costs of 25 to 33 percent. I do think we should make an important point about that. It is not so much what the percentage is, but how many dollars we get in. That is our enemy. We have kept the percentage spent on debt collection low, but we are not getting our dollars in. That is defeating the whole purpose of the program. I have chaired six hearings on debt collection in the past 2 years and we have had many agencies before us. They talk about how cost effective they actually are, as a justification for what they are doing. In the case of cost effectiveness, however, the question is: Do we ultimately get the dollars?

Here is a chart that will show what I mean. A is the Justice Department, and B is the total outside where the same amount of debt is used—$937 million—but actually we take, instead of the cost here at the Justice Department, 7.7 percent, a rough figure of 24 percent, the typical cost in the private sector. Then we take the performance here and the performance that we are actually getting over here. Here we collected $73 million from the Justice Department U.S. attorneys and $224 million over on the private sector side. It is a 25-percent cost. But the taxpayer, the Treasury, ended up with $100 million more, $68 million here, and $168 million over here. That is the bottom line that this committee is going to be looking for as we monitor this. How many dollars do we get back?

The taxpayer could care less about what percentage is up in here. Their concern is how many dollars we get. That is the way a bank operates, also. They have just got to go out and get that money back. So, in a sense, is it really cost effective to only be using that 7.7 percent figure if we just don't get the money? Again, you have got the bureaucracy. You take on people. There is an inertia there. Once you have got them, there they are. Are you ever going to get rid of them? Where with the outside agencies, I have found in my own experience, you hire people, bring them in. You don't have to build law offices, just bring them in for a job. They do it, they are out and they are through.

We have got enough here to work on for years to come. Do you want to comment on that?

Mr. MCGRATH. Yes; first of all, I agree that the critical thing is the bottom line. Indeed the first group of statistics that we started to collect were statistics on how many dollars we collected. Second, I agree that the cost to us, as a percent of collections, has probably been too low. We are actually putting more resources into this to try to get

the bottom line improved. I should point out that we will never have as good a bottom line in collecting Government loans in litigation. The Government does tend to give money to worse credit risks than others. And by the time debts get to litigation, they have gone through quite a number of steps. We end up with a high percentage of cases where there is no hope at all of ever collecting any money. I don't say that to defend the low numbers we have had. I say it to just have the record reflect that the percentages will never be the same as the collection of bad debts for a large corporation.

Senator PERCY. Thank you.

Senator D'Amato, I want to ask about your timeframe. I wonder if you could chair the hearing when I leave? We will set a new precedent. It is the first time I have been on this committee in 17 years that I have ever turned a hearing over to someone who is a nonmember. I hearby bestow upon you as a dues paid up member the honor of chairing this Governmental Affairs Subcommittee. [Laughter.]

Senator D'AMATO. I accept.

Senator PERCY. I will ask then just a few questions until I have to leave.

We asked the Department of Education to pull 15 representative cases from the 9,000 said to have sat at Justice for 3 years or more. In four of the 15 cases, the 6-year statute of limitations had expired, and the debts were uncollectable because of the delay. In eight other cases, Justice had returned the cases to Education because the addresses were not accurate. But after just a few hours of checking, Education was able to obtain correct address for four of the eight just by calling directory assistance.

Can you comment on what happened there?

Mr. MCGRATH. If I have the same 15 cases, I think that those 15 cases really reflect the historical problem. Most of those cases were referred only years after they went into default. They got to the U.S. attorney's offices in the late 1970's, early 1980's and they sat there. I have no excuses for most of these cases.

It is a sad commentary on the past. However, I have no excuses and no apologies for the past. I am only concerned about what we are doing now. In some of these cases we have actually no record of ever have gotten the case. Whether they are there or not, I don't know. I do know there is a new procedure now which requires that when cases come over, there are receipts for the cases. This problem could not happen in the future.

In other cases there were judgments that were not collectable. Beyond that, I cannot go back 4 years ago when they were referred and explain why it took such a long time. Why did the offices take a long time then? I cannot defend that.

Senator PERCY. I appreciate your candor on that. It is an example of the way the Department has been overwhelmed.

Mr. MCGRATH. I don't even know in these cases whether there was a very good excuse at the time. If there was a 3-year wait to file a lawsuit, it could well be that they determined on day 1 the person didn't have a nickel and it wasn't worth filing a lawsuit. I simply don't know at this point as to these cases.

Senator PERCY. When we are talking about debt collection in the Justice Department, are we really talking about 94 different U.S. attorney's officers?

Mr. MCGRATH. Yes.

Senator PERCY. I talked with Mr. Webb in Chicago. I think they are vigorously pursuing this with tremendous enthusiasm. They are going to develop greater respect for the Federal Government. I think some are doing extremely well. Other offices are doing somewhat poorly. In Minneapolis the U.S. Attorney has had $4.5 million in default for student for litigation in 1978 but has collected only $144,000. That is 4 percent. In Miami only $12,000 out of $1.4 million has been collected. That is less than 1 percent. Departmentwide, only $4.5 million out of $60 million has been collected.

Mr. McGrath, would you agree with me that figures like these are just unacceptable?

Mr. MCGRATH. I do, Senator. But I would like to point out one thing. I don't agree with all of the Department of Education's figures. One of the problems is their computer tends to keep adding interest on interest even long after cases have essentially been concluded in the U.S. attorney's offices, either successfully or through a decision that there is simply no blood in that stone. However, having said that, the collection figures have not been acceptable, and are still unacceptable in many offices, but all I can say is that we are giving it our highest priority to make it acceptable.

I think if you look over the last 1½ years, the improvement in a number of offices is more than acceptable and the number of offices that are being brought into line is impressive. As you say there are 94 different operations. Many of the U.S. attorneys have been more effective than others.

Senator PERCY. Thank you.

Mr. McGrath, this morning we had a discrepancy in figures between SBA and figures given to us by the Justice Department. The discrepancy appeared to be a large portion of the $574 million in loan defaults. You claim, I understand, that you have only $231 million from SBA. How do you account for that large discrepancy?

Mr. MCGRATH. The principal reason that we tend to have that kind of discrepancy is that the figures that we have given the committee are the ones that are in our bad debt docket collection system. That is, they are typically just plain bad debts. They aren't bankruptcy cases, they aren't large fraud cases or things like that. Frequently, we find that we are talking about a slightly different world than perhaps an agency is.

If we have a bankruptcy case, obviously, that gets treated totally different than just a flatout bad debt case. The other thing is that their system may have information as of a different point in time. It may reflect the addition of accrued interest over time or that kind of thing. Finally, as our systems have changed we have been putting in an automated system called Promise in many of our offices. That has been going in over the last few months. We find there are delays in getting data in our system when there is that switch over from the older systems to the newer one.

Senator PERCY. I am not sure I understand where the $350 million is, though.

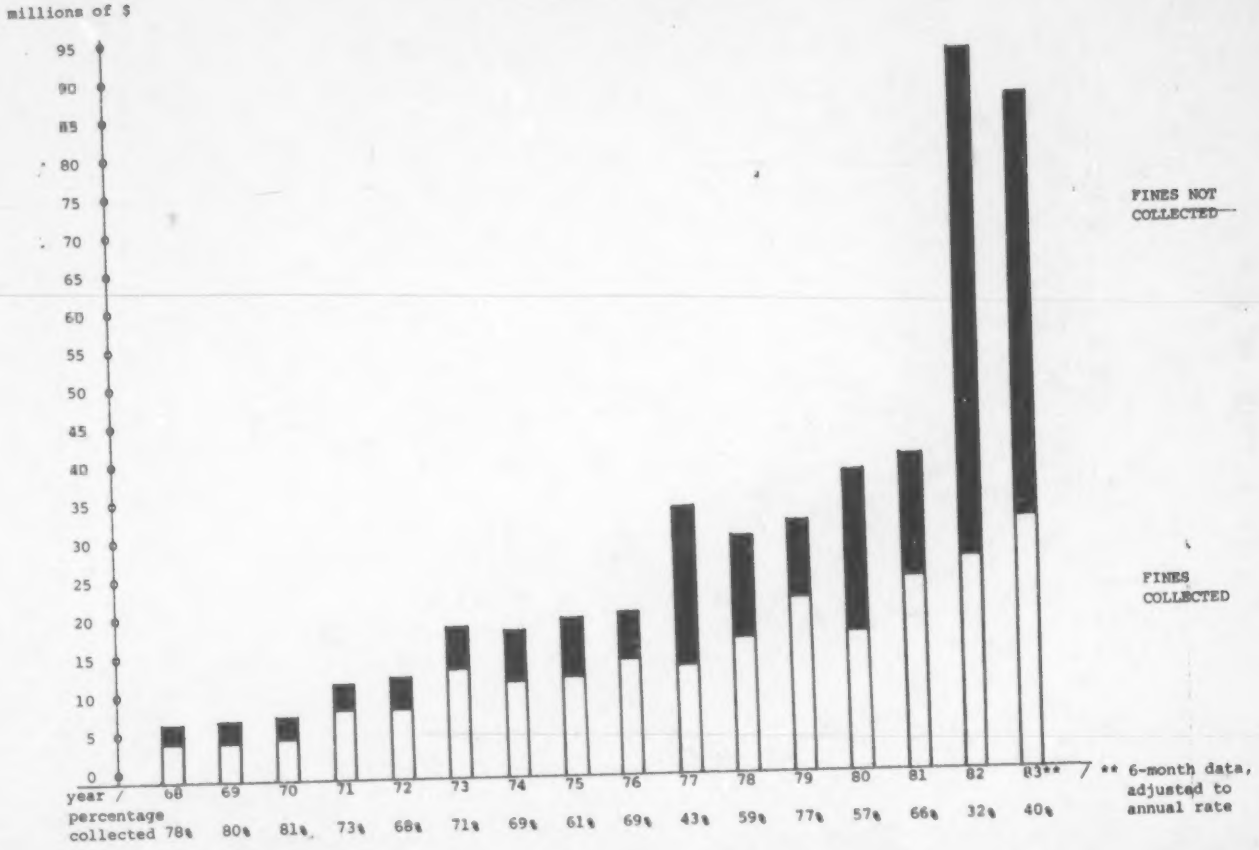
Mr. MCGRATH. The discrepancy could be in any one of those things. For example, to the extent that the agency has included—and I don't know in this case whether they have—large cases that are bankruptcies or that are fraud cases or are other cases we might conduct through the Civil Division, those would not be in our debt collection numbers. We don't consider those debt collection cases. Those are cases to be sure where somebody owes the Federal Government something. But what we do in those cases is to actually litigate.

These are typically bankruptcy proceedings or these are complicated fraud cases or something like that. Those are not just the automated run of the mill debt collection cases. They also tend to be cases with the big numbers.

Senator PERCY. The next question pertains to the criminal fine collections. We have a chart.

[The chart and explanatory table follow:]

CRIMINAL FINE COLLECTIONS



CRIMINAL FINE COLLECTIONS

year	fines*		fines collected*		fines not collected*		percentage collected
1968	6.9		5.4		1.5		78.2%
1969	6.9		5.5		1.4		79.7%
1970	7.3		5.9		1.4		80.8%
1971	11.7		8.6		3.1		73.5%
1972	12.8		8.7		4.1		68.0%
1973	19.7		14.0		5.7		71.1%
1974	17.7		12.2		5.5		68.9%
1975	20.8		12.7		8.1		61.1%
1976	21.6		14.9		6.7		69.0%
1977**	34.4	(43.0)	14.4	(18.7)	20.0	(24.3)	43.5%
1978	31.1		18.3		12.8		58.8%
1979	32.5		24.9		7.6		76.6%
1980	37.5		21.3		16.2		56.8%
1981	42.1		27.6		14.5		65.6%
1982	94.0		29.7		64.3		31.6%
1983**	87.0	(43.5)	35.0	(17.5)	52.0	(26.0)	40.2%
TOTAL	449.1		245.9		203.2		54.8%

* in millions of $

** actual data adjusted to annual rate
(unadjusted data in parentheses)

Senator PERCY. This is an internal Justice Department problem. Criminal fines are levied, after all, by judges and to the extent that we don't collect them the penalties put on criminals by Federal judges simply are not being implemented. I think we ought to have particular diligence in this area. This is a penalty that they are paying as a result of a crime against society. Over the past 16 years, barely half of all criminal fine dollars have been collected.

In the past 18 months only one-third of all fine dollars have been collected. It is a serious problem. I say it is serious because I fully expected to be subtly roasted back home on campuses all over Illinois for going after student loans. I must say I was extraordinarily pleased to find that they thought it was about time this racket ended. Maybe it is just that the people who were paying came up to date and were mad that they were paying them and others weren't. But no one came up to me and ever criticized this program.

If we can go after students and really go after them and nail them as we are now, and they are starting to pay up and they are going to take into account they have got to pay up, criminals who owe money to the Federal Government ought to realize that we are going to make life uncomfortable for them, also.

I won't ask you a question about this unless you want to make some comments on it. But I would be interested here to be certain that we are pursuing criminal debtors as well as honest citizens. I have asked the GAO to undertake a study of the whole problem of criminal fine collection. Some time this summer we might want to have a hearing on this particular aspect of debt collection. We would very much appreciate your assurance that we would have cooperation with the Justice Department in connection with any possible hearings.

Mr. MCGRATH. Absolutely. I would like to make one comment, Mr. Chairman. Criminal fines are usually levied without any relation to the ability of the criminal to pay. What happens in a very large number of cases is that either the individual never had any ability to pay the fine to begin with or once that fine gets put behind IRS liens, RICO and other forfeitures and the payment of the criminal's attorney—which usually happens up front or he doesn't have an attorney—he doesn't have any money left to pay the fine.

When you come out of that there is the problem that a large percentage of the large fines are levied on criminals who go to jail for a long time and therefore have no ability to earn money there. The fact is that many of these fines are uncollectable from day 1. I don't have any terrific confidence that the experience that this chart shows can be greatly improved upon by better collection methods. However, I do think that this is a matter that demands further study and we would be happy to cooperate with the committee.

Senator PERCY. Thank you very much.

Earlier today Senator D'Amato and I introduced legislation to allow the Justice Department to use private litigation. As we have seen with last year's Debt Collection Act, however, giving the authority to use new tools is not always enough. We need really a sense of commitment from the Justice Department that you will use private litigation as soon as legislation is enacted and that you would use it extensively. Do we have such a commitment from you on this?

Mr. McGRATH. Absolutely. And from the Attorney General.

Senator PERCY. Very good indeed. I really appreciate that very much.

I have just one final question. Five-sixths of all criminal fines go to offenders who are not sent to prison. I hope they don't pay off their fine by committing another crime. I would not encourage them to do that. But certainly we can find a system to determine where they got their money when they pay their fine. We will follow up on that, and I appreciate your support and help. Again, I want to thank you very much indeed for the opportunity we have had to work with the Justice Department on this. We have very high regard for the Attorney General.

I will have to leave now to introduce Judge Webster, another highly respected member of the Department of Justice. I thank Senator D'Amato again for your extremely fine interest in this area, your diligence and for again showing how the private sector and the public sector can work together for the common good. I am very sorry I could not join you for the final panel. But they are constituents of yours. I imagine you will take very good care of them.

Senator D'AMATO [presiding]. Mr. Chairman, thank you very much.

Mr. McGrath, pursuing Senator Percy's last question to you with regard to the introduction of the legislation that he and I have cosponsored, that which would give the agencies the ability to contract out for private litigation, reserving to the Justive Department obviously the ability to recall any case. The firm also would have to make periodic reports to you, as a matter of fact monthly reports to the Attorney General's Office.

You indicated to the chairman, Senator Percy, that you would be supportive. Is that correct?

Mr. McGRATH. We would be supportive of legislation that would give the Attorney General the right to retain private counsel. We would oppose very strongly any legislation that would give the head of any other agency the authority to retain private counsel.

Senator D'AMATO. Supposing we amend that legislation to indicate that within 30 days the Attorney General had to approve or reject the selection made by an agency of counsel?

Mr. McGRATH. I don't think that would solve the problem that really concerns us.

Senator D'AMATO. What is the problem?

Mr. McGRATH. The problem that concerns us is this. Once you get into court with litigation we believe, and history has shown, that it is very important that that litigation be under the central authority of the Attorney General. It is true that many of these loan cases will never involve questions of policy, fact, or law, of any moment. Indeed most of them will result in default judgments. Nevertheless, a number of the cases will end up involving counterclaims, or other questions of law, and we believe it is essential that the Attorney General have the immediate control so that he can get into any of those cases that he wishes and he can control the cases.

In addition, we believe it is essential——

Senator D'AMATO. If I might just for a moment. What would be the difference between the Attorney General designating a firm and an agency doing it? We are talking about collection matters here.

Mr. McGRATH. The difference would be that we have learned from very practical experience over the years that where another agency does the litigation itself, even if the Attorney General remains in nominal control, that nominal control turns out to be almost nonexistent in reality.

Senator D'AMATO. What experience has given that? What cases? You said you learned by experience. Could you cite any cases that have taken place?

Mr. McGRATH. Yes. For example, in the energy area, a good deal of the litigation enforcing the petroleum price and allocation rules of the 1970's was done by the Department of Energy.

Senator D'AMATO. Aren't we really talking about an area far different in terms of underlying dollars? We are talking here about debt collection as opposed to policy questions. Might I suggest that we are really straining to come up with the reason why this legislation should not go forth?

Mr. McGRATH. No. I think the policy should go forth. All we are saying is that the retention of counsel and therefore the supervision should be by the Attorney General.

Senator D'AMATO. I have no problem with the supervision, no problem with the Attorney General retaining control, but let me tell you, you just don't have the capacity to do it. This Senator is not convinced that you really want to do the job. This Senator is not convinced when you come in with numbers that indicate just a shocking, shocking lack of attention to this situation considering that we are the administration that says let's crack down on waste, fraud, and abuse. We have our priorities. With 94 U.S. attorney offices doing important work, of necessity they are not going to engage in debt collection for $1,000 student loan cases. I understand that.

I don't suggest that any of those U.S. attorneys are wrong. But I am suggesting that something here is wrong when we don't want to let up control. You know what it reminds me of, the battles back in town government. We couldn't manage the sanitation problems we had in the local government, disposing of garbage. Don't let somebody else come in and take that problem, who might handle it and do it well. We would rather keep the problem, not deal with it, rather than lose control. I am suggesting to you that that is what it appears like to me.

I don't think it is a coincidence that today for the first time you came forth at this hearing and even said, well, all right we will contract out. We will contract out meaning the Attorney General.

Mr. McGRATH. Senator, I disagree with your characterization of our commitment. We are committed to do this. We do intend to do it.

Senator D'AMATO. You haven't so far.

Mr. McGRATH. That isn't true. We have done a great deal to improve the situation.

Senator D'AMATO. $36 million by your own figures, these are your figures, $36 million of student loan defaults, at Justice. You have an amount paid of just over $3 million. I don't think that is doing very much. I don't think it is good enough. We have been in for more than 2 years.

Mr. McGRATH. I would submit that over the last 18 months the record has improved a tremendous amount. Bear in mind a lot of those loans

are old, old loans, where the people either can't be located or don't have the money. All I am saying is that the only fair thing in our submission is to look at the improvement over the last 18 months. You can pick out offices that aren't up to snuff yet. I agree with that. They have got to do better.

Senator D'AMATO. I am afraid you are going to have the authority and you are not going to do a darned thing. I am also afraid it is going to be a political football. I think you should have the agencies under the supervision of the Attorney General go forward and do something. I am going to tell you something. The record to date hasn't demonstrated that we are wrong.

Mr. MCGRATH. We do intend to do it, Senator.

Senator D'AMATO. Let me ask you this. What about the effectiveness of having the heads of the Federal agencies do the contracting out? Wasn't the Veterans Administration doing something in that regard? Or their counsel?

Mr. MCGRATH. The Veterans' Administration has been handling those loans under $1,200 on their own authority. I believe they have a special status.

Senator D'AMATO. Sure. What about their effectiveness? Have you had any problems? You haven't had any major policy questions with respect to the Veterans' Administration, their handling of debt collections, have you?

Mr. MCGRATH. We have no problem with their continuing that. But it is——

Senator D'AMATO. Why shouldn't other agencies be given basically that same kind of authority to contract out with the Attorney General's approval, to give you 30 days to approve or disapprove it? For example, you have final control in terms of who is selected. Why don't you say that the firm will be retained or selected in concert with both? I am not suggesting to you any pride of authorship. Senator Percy and I are willing to even change or modify the legislation to give the Attorney General input into who is selected and who is not selected.

But I think we have got to understand that this has not been a high priority item with the Attorney Generals today.

Mr. MCGRATH. It has been a very high priority.

Senator D'AMATO. I would hate to see something that is not a high priority.

Mr. MCGRATH. It has been because if you look fairly at the record of 18 months is a record we are proud of and that anybody would be proud of. What I am saying is in the area of retaining outside counsel we do intend to do it. You have my personal commitment, you have the commitment of the Attorney General. The thing we are concerned about is to let different agencies——

Senator D'AMATO. The commitment. I don't think you have the resources—personnel or computerization. I am informed that we can give you 26,000 cases. When I say "we" I am talking about all of us. We all have a stake in this together. Education has gone and surveyed 400,000 cases, and anticipate 26,000 cases to be turned over for litigation. And it is a pretty good likelihood of getting some kind of results. If we were to send over to Justice 26,000 cases, what would happen? Could they do anything?

Mr. McGRATH. It would be too many. That is why we would retain outside counsel who have the computers, the firms that specialize in this business have the computers. That is really what we need more than anything else.

Senator D'AMATO. Keep coming. Come on. You are getting there.

Mr. McGRATH. It is not a legal problem. What you need is other resources.

Senator D'AMATO. Right.

Mr. McGRATH. You need the resources of the computers, paralegals, people that get on the phone.

Senator D'AMATO. Who specializes?

Mr. McGRATH. Who specializes. We have the capacity in in many of our offices, we have been specializing in it. We don't have——

Senator D'AMATO. Excuse me. I would like you to show me what attorney, what U.S. Attorney's Office really has the capacity to undertake these kind of cases. I would suggest to you that they could spend their time much more efficiently, effectively, on behalf of the people in the United States in civil litigation, criminal litigation, et cetera. We are really coming down to saying we have scarce resources. In terms of the men out there on the battle lines. With all the kinds of problems they have to deal with, are you really going to fault the U.S. attorney who says, my God, Mr. Attorney General, I have got so many felony cases that need work on, I have got so many investigations on all kinds of complex matters, we can't blame him for saying I am not going to take 1,000, 10,000 debt cases, put it at the head of his priority list.

I don't think we have got that.

Mr. McGRATH. It doesn't really work out that way. Senator Percy suggested Dan Webb, who is a U.S. attorney in Chicago, and who has put together a group on this. He doesn't take his lawyers off RICO cases, off organized crime cases. What he has is a special unit, I have seen it, I have toured it.

Senator D'AMATO. Who?

Mr. McGRATH. Mr. Webb, the U.S. attorney in Chicago that Senator Percy referred to. He has trained paralegals and others in that office. They do the same kinds of things that a private collection firm would do.

Senator D'AMATO. You think they can do it cheaply? More effectively?

Mr. McGRATH. I don't know if you took all of these smaller cases, you have to compare the same kind of cases. Yes; I think overall they would do it somewhat less expensively.

Senator D'AMATO. There is no way. If there were any study made on it, it would be absolutely impossible because your U.S. attorneys cannot gear up for debt collection in comparison with a firm, large firm, that specializes in it. I am not advocating a large firm. But it is an absolute impossibility. You absolutely could not go forward and suggest that there would be one U.S. attorney's office in terms of cost effectiveness, return on any measurable standard, that could compete.

It just can't be because of the cost of overhead, where the emphasis has to be. Set up a three-man shop, three paralegals? Are we serious about this? The volume coming into any of these offices could not

sustain it. It doesn't make economic sense. But be that as it may, in Florida in all 1982, forget how many millions of dollars are outstanding, you didn't have one penny of collection. Why? They have got an epidemic down there. They have a crime wave. Are we going to blame the U.S. attorney there, fault him, for saying our priorities are on the battlefield in dealing with the international drug problem that is coming in.

I am not going to do that. I think it is silly to say that you can do it. Albuquerque, maybe? I don't think so. It doesn't look too good there, either.

Mr. McGRATH. If you are talking about the southern district of Florida, I don't doubt that is one of the areas where it would be most likely that private counsel would be needed. Stan Marcus, one of the top U.S. attorneys in the country, has been overwhelmed with other things.

Senator D'AMATO. And it is going to continue to be. That problem is not going to go away.

Mr. McGRATH. I am afraid it is not in the near future. That is true. But there are a number of offices that have geared up, there are others that aren't. I would suggest one thing the committee might want to do is actually view some of the offices that have gotten up to speed.

Senator D'AMATO. I understand. I would suggest the committee really is interested, this particular Senator—I can't talk for the committee—in seeing that we really get some support from Justice rather than have us drag you—and we will—through the legislative process. With all the give and take, shoving back and forth, we are going to get to the point where we are going to be able to contract out, and I think there must be input from the agencies. I am not suggesting that the attorney generals should not be involved closely in the selection, in the input, in the review. I am going to ask you to meet with us in that kind of spirit, we are not too far apart.

Mr. McGRATH. I think that is right.

Senator D'AMATO. With the bill that Senator Percy and I put in today, we are not far apart from your offer. I think we can meet your objective. I am asking you if you are willing to move in that kind of spirit to close that gap?

Mr. McGRATH. More than willing. I am eager to. I think we have to solve this problem.

Senator D'AMATO. Good. Let's not pursue that any further. We will close on a positive note.

The highest average collection per contact in the Department of Education belongs to Mr. Hastings. Were you aware of that?

Mr. McGRATH. No.

Senator D'AMATO. It is true. They have a scorecard over there in terms of how much money they collect per case. Mr. Hastings has the highest average to date. Would you tell the committee, Mr. Hastings, how this came about?

Mr. HASTINGS. The cost effectiveness of employees as collectors. I would be happy to. This happened to be a case where actually it is how I got involved in this whole question quite frankly.

We were meeting with our collection agencies to review the progress. I was beating them up without any unhappiness about the lack

of progress we were making. That was when they brought to my attention that we had a real gap here in the total system because of our lack of effective litigation posture. One of the agencies happened to mention that—

> We have got a lieutenant colonel in the Army who is a doctor who owns seven pieces of property, has all sorts of rental income, just absolutely refuses to pay his debt. They could only tell him, we will have to refer this to the Department of Education, who is going to turn it over to the Department of Justice and somebody is going to take you to court.

That guy says they have been telling me that for 10 years and nobody has done it yet. So, I finally out of exasperation said give me the man's name, rank, social security number. I was buck sergeant in the Army and was thrilled at the prospect of calling a lieutenant colonel. They did. I called the gentleman up and we proceeded to have a half hour conversation on whether or not he was going to pay his debt. He told me that he thought that we were so incompetent that he would like to have us on "60 Minutes."

I suggested that I would be willing to call Mike Wallace myself since the gentleman obviously was not a man of his word since he hasn't paid his obligation; second, he was a Federal employee; and third, I didn't think the folks would be terribly amused by the fact that a doctor who is making over $50,000 a year and had rental property wasn't paying back $11,500. The long and short of it is that since we are not bound by the Fair Debt Collection Practices Act, I advised I was able to do some things that our collection agencies weren't, and within 7 days a check was received in full.

That is my only account that I have ever personally collected and it is certainly the highest average balance that we have received by a Department employee.

Senator D'AMATO. Therefore, you now have the highest debt collection ratio [laughter] in the Department of Education, probably the entire Federal Government. We commend you on that. I think our Assistant Attorney General McGrath is looking actually with glowing eyes. Maybe he is going to take you over.

Mr. MCGRATH. Make a job offer. [Laughter.]

Senator D'AMATO. I want to thank you for coming in.

Time is moving on. We do have another panel. I would hope that as the Assistant Attorney General in charge of this area you can refine this. I am certainly willing to make the necessary amendments to accommodate Justice. I want to be assured so that we can get the kind of input which is necessary. I think in the selection, in the review, but I also think that we have got to see to it that some of the agencies have that ability I think to work with you no this.

I think if we can do that, we can satisfy everyone.

Mr. MCGRATH. I would like to do that.

Senator D'AMATO. Thank you very much.

[The prepared statements of Messrs. Olmo and McGrath follow:]

STATEMENT BY RALPH OLMO, COMPTROLLER
U.S. DEPARTMENT OF EDUCATION
BEFORE THE SENATE SUBCOMMITTEE ON ENERGY, NUCLEAR PROLIFERATION,
AND GOVERNMENT AFFAIRS ON LOAN COLLECTION

Mr. Chairman and Members of the Subcommittee:
We appreciate the opportunity to be here today to discuss with the Subcommittee our student loan collection program.

We would like to compliment you Mr. Chairman, and the other members of the Subcommittee, for your strong support of the recently enacted Debt Collection Act of 1982 (P.L. 97-365). This Act has been instrumental to our efforts to strengthen our credit management program.

The Education Department is moving rapidly to implement the provisions of the Debt Collection Act. I would like to outline the steps we have taken to exercise the authorities contained in the following three key provisions of that legislation.

o First, the Debt Collection Act Provides Authority to Refer Delinquent Borrowers to Credit Bureaus. To Implement this Provision:

- ED has negotiated agreements with major credit bureaus for nationwide coverage with respect to Federal Insured Student Loan (FISL) and National Direct Student Loan (NDSL) defaults assigned to the Department for collection.

- ED has established administrative procedures and systems necessary for credit bureau reporting on these defaults.

- ED will refer approximately 500,000 defaulted FISL and NDSL accounts this year.

o Second, The Debt Collection Act Authorizes Salary Offset Against Federal Employees Who are Defaulted on Student Loan Repayments. To Implement this Provision:

- ED has run a Federal employee computer match that identified 46,860 Federal employees in default on $67.7 million in student loans.

- We have sent initial contact letters to these individuals at the best home address available.

- As of May 2 of this year, we have received payments in excess of $2.3 million on 7,248 of these accounts. A total of 1,341 accounts have been paid in full.

- A proposed regulation was issued on May 24 to establish the procedures ED will use to collect from Federal employees with defaulted student loans by means of salary offset.

- Secretary Bell will brief the Cabinet Council in the near future on the Administration's overall strategy for mandatory offset recovery of outstanding loan receivables. The cooperation of other Federal agencies has contributed greatly to the project so far. We feel confident that recoveries in 1983 will justify the untiring efforts of this Subcommittee, in particular, and other members of Congress.

o Third, the Act Authorizes Contracting with the Private Sector for Collection Services. To Implement this Provision:

- ED has fully implemented two major private sector collection agency contracts. The first major cohort of student loan paper was transferred to the collection agencies in January, 1982.

- Since that time, we have transferred 400,000 accounts to the two contractors at approximately $637 million.

By March of this year, ED employee collectors working together with the private collection agencies collected an all time high monthly total of $7.4 million on defaulted student loans. This total exceeded the previous high by $1.5 million.

Overall, FY 1983 collections from major Federal education programs are increasing substantially over FY 1982 collections. We have compared collections in FY 1982 and FY 1983 for the two major programs where the Education Department is principally responsible for default collections — the Federally Insured Student Loan (FISL) and the National Direct Student Loan (NDSL) programs. We estimate that repayments will increase from $55 million in FY 1982 to $72 million in FY 1983 for a $17 million (31%) increase.

In respect to the Cuban Student Loan Program, we would like to highlight some of the management improvements being instituted to increase collections. First, since last fall, we have increased sixfold the number of staff dedicated to collections in this program from 2 to 12.

Second, we have tested a high impact mail campaign which has resulted in positive responses from better than 75 percent of the first 1,860 demands generated. Over just the past five months, we have recovered $506,000 and we expect to collect a total of $1.4 million by the end of this year which is more than twice the amount collected last year. This success rate suggests that our recoveries should substantially increase as we continue the mail campaign. We will do so by June through a private contractor on the additional 5,400 accounts for which we have recently secured fresh addresses from the Internal Revenue Service.

Third, accounts on which we are initially unsuccessful in collecting will be included in another contract for collections which we will let to the private sector late this year. The Department has drafted a Request for Proposal (RFP) for this collection contract, and we expect to publish the RFP this summer and negotiate the final award this year. The projected success on this program should lead to retirement of most of the Cuban Student Loan Program portfolio by FY 1986.

Besides these debt collection initiatives, there is another important credit management tool that merits discussion. This tool is the aggressive litigation of cases involving delinquent borrowers. We have known for some time that there some recipients of Federal loans who feel no sense of

responsibility to repay these funds, even though they are perfectly capable of doing so. We are frequently informed by our contract collection agencies of instances where they have been able to locate the debtor, have spoken to him or her, and have been told, in effect, to get lost.

Under our current procedures, the collection agency then tells the debtor that it intends to refer the account back to the Department of Education with a recommendation for litigation. Under the Fair Debt Collection Practices Act, the private collection agency is subject to penalty if it were to be more assertive with respect to the possibility of litigation.

Currently, once the account is referred back to the Department of Education we must rely solely on the various United States Attorneys' Offices to pursue litigation on student loan accounts. There have been long delays in getting judgments on some of these accounts due to such factors as:

- o crowded Federal court dockets.
- o complicated administrative procedures to refer accounts from ED to Justice.
- o reluctance by some U.S. Attorneys to pursue small balance referrals.

We believe that the threat of prompt litigation in those instances where such action is warranted will have positive effects. In the short term, we will be able to secure and enforce judgments in those cases where people have the ability to pay but have simply refused to honor their obligations. In the long term, the deterrent value of prompt litigation will stand as a reminder to those who are tempted to ignore their debts.

Just recently we surveyed our collection contractors and counted more than 26,000 cases which could, given time, be prepared for litigation in major metropolitan areas. These cases would be in addition to the more than 22,000 cases, at approximately $48 million, that we have already referred to the Department of Justice.

Although we are capable of transmitting electronically much of the case information needed to the U.S. Attorneys' Offices, many of their offices do not have the technology to accept such information electronically. The process of transmitting data manually is time-consuming and costly.

We believe that the interests of the American taxpayer will be best served by amending the Debt Collection Act to authorize the Attorney General to contract with the private sector for litigation services and to pay for these services out of the collections proceeds. We support the proposed amendment presented in the Department of Justice testimony today which would authorize the Attorney General to obtain private counsel.

If the Attorney General is given authority to procure litigation services for defaulted student loan notes, there will be a great need for consultation with the Department of Education in the development of the contract management procedures. This is important in order to assure close coordination between the two Departments and to ensure timely and effective judgments on defaulted student assistance claims.

If the Attorney General is not given authority to procure private sector litigation services, the Education Department would then be best served by authorizing the Secretary of Education — first on a pilot basis — to contract with private attorneys for the litigation of these defaulted student loan accounts.

Finally, the Education Department will soon be transmitting the Student Loan Collection Improvement Amendments of 1983 to further strengthen our capacity to manage our receivables portfolios. These amendments, which are primarily to the Higher Education Act, build on the Subcommittee's important efforts begun last year with the passage of the Debt Collection Act. We look forward to working with the Subcommittee for the enactment of these proposals.

Mr. Chairman, I hope that this testimony has been responsive to the concerns of your Subcommittee. We appreciate the support your Subcommittee has given the Department's loan collection efforts and look forward to your continued support on other loan collection initiatives. I will be pleased to respond to any questions the Subcommittee may have.

STATEMENT

OF

J. PAUL McGRATH
ASSISTANT ATTORNEY GENERAL
CIVIL DIVISION

Thank you Mr. Chairman. It is a pleasure to be here to discuss the Justice Department's efforts in the area of debt collection and to suggest a legislative proposal that could enhance the government's ability to collect hundreds of thousands of delinquent debts. I can assure you that, in the last year-and-a-half, we have made a major, and I believe successful, effort to recover monies owed the government.

First, I would like to briefly discuss this Administration's record in the area of debt collection. As you know, the Administration and the Attorney General have assigned great importance to the task of collecting debts owed to the United States. While the Attorney General asked me to coordinate the Department's collection efforts, it is the U.S. Attorneys throughout the country who are in the front lines of this effort.

I am happy to report that we have compiled a remarkable record of success in our debt collection activities. During fiscal year 1982, U.S. Attorneys recovered $151 million in cash on delinquent civil debts and criminal fines. During the same period, the litigating divisions in Washington - Antitrust, Civil, Tax and Lands and Natural Resources - collected an additional $48 million for a total of just over $200 million. In the first six months of FY 1983, the U.S. Attorneys report receiving $83 million, a $23 million increase over the comparable period in 1982.

Since the initiation of our debt collection effort, we have taken the following actions:

- Met individually with each of the 94 U.S. Attorneys to impress upon them the Attorney General's commitment to collections and extracted from them commitments to take a personal interest in improving their debt collection operations.

- Determined which U.S. Attorneys needed more resources in their collections units and Deputy Attorney General approved allocation of positions and modern word processing equipment to U.S. Attorneys' Offices which most needed help. At this point, the majority of U.S. Attorneys have either computer supported systems or automated word processing systems devoted to collections work. By October 1, 1984, every U.S. Attorney should have computer-supported or sophisticated records systems for debt collection. When these systems are operating, we should be able to generate automated periodic progress reports to track the progress of our collections efforts by U.S. Attorney's district, by agency, by debtor, or by almost any conceivable measure.

- Conducted week-long training conferences for collections personnel in U.S. Attorneys' Offices. In FY 1982, 165 AUSAs and collections clerks attended these training

programs and completed over 5,184 hours of concentrated instruction in modern debt collection techniques. We are following up this formal training with a program in which outstanding collections clerks from selected offices are visiting U.S. Attorneys' Offices with collections problems to apply their expertise to the situation and help devise solutions.

- Training sessions were also held for representatives from our client agencies to inform them of the data which must be sent to the U.S. Attorneys to enable them to collect the agencies' delinquent debts. From these meetings and with the help of OMB and GAO, we devised the Claims Collection Litigation Report for use by all agencies sending us debts to collect. The report standardizes the format for the debtor information needed for the U.S. Attorneys to collect these moneys.

- Encouraged U.S. Attorneys to file large groups of collections cases simultaneously to generate media coverage of our collections efforts. Mass filings, the impoundment of debtors' cars and similar events received wide publicity and have helped to let the public know that this Administration is serious about collecting the delinquent debts owed the U.S.

- Finally, we decided to count cash collected as the best interim measure of our progress. We realized that such a measure did not capture all of the U.S. Attorneys' collection activities such as forfeitures and foreclosures, but cash was easy to count and it represented a real recovery for the U.S. as opposed to the sometimes inflated value of forfeited collateral or foreclosed assets which might not be liquidated until sometime in the future and even then for an uncertain amount.

Our top priority for FY 1983 has been implementation of a direct deposit or lockbox system. We found that the U.S. Attorneys were sending money they collected back to the creditor agencies and that weeks, and sometimes even months, went by before collected checks were deposited. A study showed that the U.S. could save approximately $1.2 million in interest on this float if we could get the money into the Treasury faster. With the help of OMB and the Treasury Department, we are on the verge of implementing a system pursuant to which every dollar we collect will be sent daily to a lockbox. The bank operating this system will get the funds to the Treasury the day after it receives them. Justice will thereafter transfer debits and credits to keep the system in balance. Not only will this system get the cash into the Treasury much sooner but it should also provide almost instantaneous data on what we have collected for each agency on each debt sent to us for litigation.

The enactment of the Debt Collection Act of 1982 has greatly enhanced the ability of federal agencies to collect debts owed them. This Committee, and especially you, Mr. Chairman, are to be congratulated for your role in enacting this important legislation. Authorizing the use of private collection agencies to recover debts should be an especially effective tool in recovering on many debts which before had been largely uncollectable.

Indeed, potential litigation arising from the use of this collection tool has created a problem for our debt collection team at the Justice Department. Because this enormous backlog of cases is now coming over to us, we find our resources severely taxed in attempting to bring all meritorious cases in a timely fashion. We estimate that the U.S. Attorneys can handle 2,000 new cases a month, but the number some are predicting will be referred to us, especially of delinquent student loans, far exceeds that. If we are to aggressively prosecute those cases where private collection efforts have proved unavailing, we need to supplement our resources in this area.

Short of enormously increasing the size of the U.S. Attorneys' offices, the only viable solution is to retain private firms to handle the overflow of this massive influx of cases. However, our review of the law in this area suggests that the Attorney General or the head of any department may not have the authority to pursue such a course. Further, under current law, we are expressly precluded from contracting on a contingent fee basis. Therefore, Mr. Chairman, if we are to follow through on the impressive start we have made in debt collection, we need

legislative authority to retain private counsel for the limited purpose of collecting debts.

The legislation attached as Appendix A to my testimony would provide the Attorney General with authority to retain private counsel for the limited purpose of collecting claims referred to him pursuant to section 13 of the Debt Collection Act. 31 U.S.C. 952(f). In addition, the legislation will permit private counsel to be reimbursed out of the proceeds of the collections, thereby permitting us to retain counsel on a contingent fee basis. Private counsel appointed pursuant to this grant of authority would still be supervised by responsible Justice Department officials, or by agency attorneys where appropriate. We could thereby ensure that they vigorously pursue these cases, comply with applicable federal statutes and preserve appropriate legal defenses of the United States.

This proposal has a number of advantages over alternatives which attempt to shift resources to handle these cases within the government. First, although the bulk of the current caseload backlog is in the area of student loans, as other agencies begin to use the authority granted by the Debt Collection Act, more cases will be referred to us. For instance, we have been told that HUD has a backlog of some 50,000 home improvement loans where this authority might prove useful. Therefore, rather than addressing this problem on a program-by-program basis, we believe it would be advisable to grant the Attorney General the authority to retain private counsel for any case arising from a referral under the Debt Collection Act. This would be in keeping with the Debt Collection Act which also took a government-wide approach to this problem.

Secondly, Mr. Chairman, we believe that it is important that the Attorney General retain the flexibility to employ private counsel only where necessary, and continue to utilize the local United States Attorneys wherever possible. Not only does the use of United States Attorneys assure greater control over this debt collection activity, but it also is much more cost effective. Our data indicates that the average contingent fee contract in commercial debt collection litigation ranges from 25% to 33 1/3%. In contrast, during FY 1982, U.S. Attorneys have collected $16.28 for every dollar spent on debt collection; in effect, a mere 6% "contingent fee". Wherever possible, therefore, we would like to continue using our U.S. Attorneys, retaining private counsel only in those localities, usually in major cities, where the number of debt collection cases would overwhelm our resources.

Finally, providing the Attorney General with the authority to retain private counsel in debt collection cases would permit Justice Department officials to review any such cases in order to ensure conformity with the government's position in other debt collection matters.

This is consistent with the major function of the Department of Justice, pursuant to 28 U.S.C. §§516 and 519, which is to resolve any differing agency perspectives in litigation-related matters, and present the position which best serves the government's overall interest.

The collection cases which would be handled by private counsel would, for the most part, involve recurring and somewhat simple factual and legal issues. However, on occasion it may be

necessary to protect important priorities or defenses, such as sovereign immunity, available to the United States. Therefore, supervision by the Department of Justice, using its litigating authority, will be of great importance to the proper handling of these cases.

In conclusion, Mr. Chairman, we would urge you to amend the Debt Collection Act to grant the Attorney General the authority to retain private counsel in these cases. If granted this authority, I can assure you that the Justice Department will see to it that every meritorious claim received from the agencies is vigorously prosecuted. I would be happy to answer any questions you might have.

APPENDIX 1

PROPOSED AMENDMENT TO 31 U.S.C. 3711

Section 3 of the Federal Claims Collection Act (31 U.S.C. 3711) is amended by renumbering subsection (g) as subsection (h) and adding the following new subsection:

"(g) Notwithstanding any other provision of law, the Attorney General is hereby authorized to retain private counsel, under such terms and conditions as he determines appropriate, to handle litigation to collect claims referred to him for legal action pursuant to subsection (f)(1) and to pay such counsel out of the proceeds of such litigation."

Senator D'AMATO. For our final panel, I would like to welcome Mr. Bernard D. Landau of the law firm of Hayt, Hayt & Landau, and Mr. Bob Dawson of G C Services.

I have asked Mr. Landau and Mr. Dawson here this morning to tell us how the private sector can assist the Federal Government in collecting and litigating these debts.

If I may, I ask you to summarize your testimony for us. It always happens that those who have been chosen as the fourth panel get shortchanged and they come from the longest and farthest places.

We certainly apologize for having you wait. I think there are important matters that we have to touch on here.

So, Mr. Laudau, if you will, summarize your testimony. All of your remarks will be included in the record as if read in their entirety.

TESTIMONY OF BERNARD D. LANDAU, ATTORNEY, HAYT, HAYT & LANDAU, NEW YORK, N.Y.; ALAN D. REFFKIN AND ROBERT S. LEWINTER, PARTNERS OF BERNARD D. LANDAU; G. L. DAWSON, ASSISTANT VICE PRESIDENT, G C SERVICES CORP., HOUSTON, TEX., ACCOMPANIED BY ED BURKE, CORPORATE COUNSEL, AND CAROLYN WEBBER, WASHINGTON REPRESENTATIVE

Mr. LANDAU. Senator D'Amato, in your capacity as acting chairman, I wish to thank you and Senator Percy for giving us the opportunity to appear here today and to present certain testimony which we hope will shed some light on the immediate problem.

Accompanying me here today are two of my partners, who are heavily involved in the area of collection, for our firm, Allen D. Reffkin, sitting immediately to my right, who is the resident partner of our Washington, D.C., office, and Robert S. LeWinter, who is the partner of the firm involved in the student loan portfolio, which we are handling at the present time for a large number of State guarantee agencies.

I consider it a privilege and an honor to appear before this committee and I hope that the information I am presenting to you today will shed some light on the need for litigation, by the private sector of attorneys. The feasibility of this type of program and the effectiveness that this type of program will have upon the debts owing to the U.S. Government.

In order to support my statements, I would like to give some brief background information on our firm which has been heavily involved in the area of legal debt collection for the past 27 years.

I am the senior and managing partner of the national law firm of Hayt, Hayt & Landau, and we presently employ over 750 people, including 85 attorneys, 34 of whom are partners of our firm.

We have 16 offices in 11 States and Washington, D.C. Interestingly enough, many of the areas that have been addressed today as being problem areas of debt collection on the student loan portfolio, are locations where we are presently maintaining operations.

When I joined the firm in 1955, the firm was involved in collection and was heavily dependent upon manual systems, as the Department of Justice and other organizations are dependent today.

In 1966, we had the foresight to address the area of computerization. From 1966 until the present time, our firm has been computerized. As a law firm, as well as many other law firms in the private sector of this country, we have the capacity to deal with the issue of debt collection through the support of computers.

Our firm in the past 10 years has received millions of dollars of accounts as well as millions of accounts themselves. In the past 10 years, we have received approximately $2.5 million in accounts with a total dollar value of approximately $1.2 billion.

In 1982 alone, on a national basis, our firm received 365,000 accounts with a total value of $355 million and collected approximately, one firm, $85.2 million. Our ultimate liquidation on consumer debt accounts is approximately 38 percent over a 2-year period.

The issue, being addressed this morning by various members of the panel, as well as Senator Percy himself, addresses the issue of the immediacy of litigation. I think that is the key issue, as well as the capacity of the Department of Justice, that has the ultimate authority and responsibility today to deal with the volume of accounts that will be received in the immediate future that will require litigation.

The area of debt collection, based upon 27 years of experience in this field, falls into three areas. The first area, the Federal agencies:

The Federal agencies have the responsibility as they have in the past to make a determination as to who should receive the particular loan or whatever the situation is that is resulting in moneys being expended by the Federal Government. That agency is not a collection agency. It should not encompass the responsibility on a continuing basis to collect the bad debts that eventually ensue within their particular agency.

The area of collection agencies, outside collection agencies, is an important factor and continues to play an important factor in the collection of delinquent debts. However, when you stop short and the collection agency is not in the position to pursue legal action within a period of 18 months or 2 years the program fails. The necessity of instituting legal action on a timely basis, as far as we are concerned, as a law firm, is within 7 to 10 days from the time that that determination is made.

We are dealing with a very mobile society in the United States. Information today is of great value and by virtue of that information, legal action can be instituted and result in liquidation. It cannot be done on a piecemeal basis. Over the coming years, just dealing with the Department of Education, we estimate that approximately 35 to 40 percent of the total number of claims that would be placed with private collection agencies will require litigation. This translates itself into 350,000 lawsuits.

The instituting of the lawsuit is only the initial step that has to be taken. As you aptly pointed out to Mr. McGrath, a large percentage of these claims just go by default. In the area of consumer debt collection, approximately 95 percent of claims go by default. All that is necessary to institute the suit against that responsible party is a limited amount of information and once that is passed over to the private sector attorneys, legal action can be instituted and judgments secured.

There were certain examples given by Senator Percy regarding a particular physician and his failure to make payment. We in our experience have had a situation where an orthopedist physician owed

$20,000 on a claim. When we contacted him, he offered to pay the account off on the basis of $200 a month. We sued him, got a judgment against him and after we got a judgment against him, he paid the $20,000 in full in one payment.

There have been many other situations involving people who have served in the capacity of county attorneys in various States who have refused to make payment. Individuals who worked for the offices of State Governors, who refused to make payment and in each one of these situations, it was necessary for us to institute legal action. And until the legal action was instituted and at that point, they even awaited the entry of a default judgment and when the default judgment was entered, they finally came forth and paid the claim. It is not really a matter of numbers that we are addressing ourselves to, it is a matter as to how many lawsuits. It is the ability of the Department of Justice or the private sector in bringing litigation within a proper timeframe and the proper timeframe in my experience and over the last 11 years, that we have represented numerous municipalities, and we have gone through the exact same problem is timely litigation.

Senator D'AMATO. I am wondering if you could in the next minute or two hone in on your experience, not only in debt collection matters, but particularly with regard to student debt collection.

What experience have you had in that area? If you sue a commercial client as opposed to someone in the student area, there might be some difference.

Mr. LANDAU. At the present time we have a portfolio of 400,000 files. Of those 400,000 files, 95 percent involve consumer debtors. A percentage of those consumer debtors involve the defaulted student loans. The defaulted student loan, unfortunately, gets grouped in the entire gamut of defaulted consumer debts. A lower percentage of liquidation is placed upon the student loan and I feel this is not appropriate.

The reason I make that statement is that, generally, when you are dealing with a student loan the individual is one who is educated, many of these individuals have gone on to finish their education, and as time passes, one thing that is unique about a student loan, it is like a wine the older the claim, it becomes more collectible. The longer it lies there, if it is a period of 4 or 5 years before the default occurs, the possibilities or the probability of collecting against that individual increases dramatically.

Senator D'AMATO. Do you represent various universities and State agencies in collection work with regard to defualt of student loans?

Mr. LANDAU. Yes; we represent at the present time approximately 27 State guarantee agencies as well as individual universities.

Senator D'AMATO. From the date that the process takes place and your firm gets a case could you describe briefly for the committee what you do, what the success ratio is in terms of recoveries?

Do you or any of your partners have that information?

Mr. LANDAU. I am familiar with the information requested.

Senator D'AMATO. Would you give it to us, please?

Mr. LANDAU. As far as what we receive from the various 27 agencies that we represent on a national basis——

Senator D'AMATO. What kinds of agencies?

Mr. LANDAU. State guarantee agencies. Rhode Island Higher Education Assistance Authority, the New Jersey Higher Education Assistance Authority, Massachusetts, Pennsylvania——

Senator D'AMATO. Do many of these agencies deal with the Federal Government? Would you describe how they act and how those moneys come to them?

Mr. LANDAU. As far as their particular transactions?

Senator D'AMATO. Yes.

Mr. LANDAU. On their particular transactions, they are generally working, I believe, with a bank. The bank is making the loan. They are, then, looking to the State guarantee agency, then, in turn, the State guaranteeing agency would be looking to the Federal Government.

Senator D'AMATO. Federally insured programs. They are insuring for the banks and then the agencies themselves contact you?

Mr. LANDAU. Correct.

Senator D'AMATO. When they contact you, would you describe the process, the ordinary process by which your firm comes in to play and what you do?

Mr. LANDAU. Once the account has reached the default status as far as the agency, the client is concerned——

Senator D'AMATO. The agencies being State education agencies in certain cases?

Mr. LANDAU. That is correct, as well as the guarantee authorities. Once that determination is made, the account is then turned over to us. It is turned over to us computer to computer, meaning that the actual data is contained on a magnetic tape.

That tape has all the necessary information which we need. With other agencies, it is necessary that we take hard copy. That hard copy or the computer to computer referral data is received, it is entered into our computer within a period of 24 hours and within 24 hours, a demand letter will be sent out to the debtor.

We will generally wait for a period of 3 days. If within 3 days we do not receive a response, a telephone call will be made to the debtor; if we are able to make contact with that debtor and were not able to work out a settlement, seeking the arrearage to be brought current, or if the situation is where we are seeking the total payment, there is a refusal on the part of the debtor to make payment, a determination is made by an attorney or a paralegal individual that that party should be sued.

The transaction is entered into the computer and on what is called an update, when we pass all 400,000 files, a summons and complaint will be prepared and issued and sent out to the appropriate process server or constable, to serve the process. Our capacity is that on any one day we could produce 23,000 summonses and complaints.

Senator D'AMATO. Mr. McGrath is no longer with us.

Mr. Ford, are you still here?

Mr. Ford, come on up here. How lucky we are. [Laughter.]

Mr. FORD. Yes, sir.

Senator D'AMATO. How does that sound? We were talking about who could be more efficient and effective in debt collection.

Can the Justice Department do something like that?

Mr. FORD. I don't think there is any doubt we could, given the 15 years that has taken to develop this system. Please don't misunderstand.

Senator D'AMATO. You mean it takes 15 years to undertake?

Mr. FORD. I think we could probably get it a little faster. Bernie admitted that we could learn. Don't misunderstand me. I am a big fan of this system. He has made a presentation to us. We think at least——

Senator D'AMATO. I am not advocating for him. I advocate for the approach.

Go ahead.

Mr. FORD. The system approach from what I have seen, from the presentations, Mr. Landau has made to us, seems to be certainly the state-of-the-art in the area.

Senator D'AMATO. Where we should go?

Mr. FORD. We certainly think law firms like Mr. Landau's should be the kind of firms that the Attorney General should be authorized to retain, to handle the litigation in the debt collection area.

Yes, Senator.

Senator D'AMATO. It seems to me rather apparent that these are the kinds of things that we should be able to move toward and improve governmental operations and efficiency so that we can use our scarce resources where the highest priorities are. Yet, when we take the totality of all of these $1,000, $2,000, $3,000 defaults, bad loans, it adds up to a significant amount. That is a rather significant dollar amount. That is why we just cannot turn our back on it.

Individually, they may not be important, but we keep repeating the abuse. It becomes an important deficiency that we must deal with.

I thank you for your candor. I really do.

I think you made an excellent presentation, Mr. Landau, and I thank you for having come down and spent so much of your time on this issue.

We have made great progress in this area under Senator Percy's leadership. He has been a pioneer in this area, coming to the point where we now have Justice coming forward and indicating that it is ready to move in a certain direction. I think we may be able to get a bill which has administration support.

I would like to get the most effective bill possible on the books and into action so that we process those 26,000 cases that the Education Department has got but there is no one who has the capacity within the Federal Government to deal with them.

It doesn't make much sense if you went out and identified 26,000 cases and are not going to do anything.

Mr. Dawson, if you would summarize your statement?

Mr. DAWSON. My name is Bob Dawson. I am vice-president of G C Services Corp.

Senator, with me is Ed Burke, who is our corporate counsel: G C Services and Carolyn Weber, one of our Washington representatives.

You have a complete testimony that we have submitted.

I will very briefly cover some of the key points that differ from those previously stated rather than reinforce the points that already have been made.

We would like to express our gratitude and full support of the commitment this administration has made to recover the debts owed to the Government. G C Services is especially pleased with the efforts

of OMB to create reform 88 which goes beyond debt collection to improve receivable management, and with the recent passage of S. 376 which would give U.S. Government agencies the authority to pay collection agencies on a contingency basis rather than with appropriated funds.

With respect to the use of third party litigation outside of the Government, we concur with the items addressed by the previous speaker, the Department of Education and OMB. But there are two parts to this entire litigation question. Not only is there less clout at this time.

G C Services has two of the contracts from the Department of Education to collect defaulted student loans. We also are installing an automated collection system for the IRS. Therefore, we have had significant experience in dealing with two sides of Federal debt collection. We find that not only is there a $1 billion backlog in litigation waiting at Justice to be sued, but the second side of the picture is judgment enforcement.

At the present time there is no department that has line responsibility in the Department of Justice for judgment enforcement.

Our understanding is that the Department of Justice has nearly $3 billion in judgments that are awaiting some type of enforcement action on the judgments.

The judgments are just the first step in the picture. Enforcement needs to take place from there.

Senator D'AMATO. That is interesting. It is just not a matter of bringing suit as you pointed out, it is getting judgment and all of those things leading up to the judgment and enforcement with some reasonable effort. That kind of enforcement effort is necessary to make sense out of it.

How deficient in this area—are you in the position to make some kind of an estimate with respect to the $3 billion in judgments that have been obtained?

How much do you think could be collected with some reasonable effort given, reasonable attention to that area?

Mr. DAWSON. If they were our accounts, I could, but I have not seen the accounts that the Department of Justice has. We take the attitude as does the industry in general that not just anyone is sued. Assets are located before action is taken to file suit. That is not always the case.

Senator D'AMATO. Mr. Landau, with regard to that particular point, so that the record reflects it, is that also the manner in which you operate?

Mr. LANDAU. Yes; we will not institute a lawsuit against an individual who we feel would be merely recovering a judgment which is uncollectable.

Senator D'AMATO. Do you make a notation after having gone through a procedure that you do not believe that this is worthwhile pursuing because the person for all intents and purposes is judgment proof?

Mr. LANDAU. If you are referring to the $1 billion, I have no idea as to what the basis of litigation was.

Senator D'AMATO. Wait. You are a good lawyer. [Laughter.] Go easy.

Mr. Dawson indicated that they just don't sue everyone. There may be a claim that is due for $1,000, $2,000, $3,000, debt due and owing, that they ascertain not only that it is due and owing, where the person is, et cetera, but whether or not that person, there is any reasonable degree of collecting moneys before they institute a lawsuit; is that correct?

Mr. DAWSON. That is correct.

Senator D'AMATO. Do you utilize that same policy before you bring a suit?

Mr. LANDAU. We follow a similar procedure and not knowing exactly what Mr. Dawson's procedure is, I would have to assume that our procedure probably goes slightly beyond.

We institute the suit. In Mr. Dawson's situation, they are an agency and not instituting a suit. We as a law firm, our relationship is one of attorney-client with every client that we represent. Before we institute a suit, we go through an asset investigation. The majority of our reputation has been through the years the reputation of not-for-profit organizations and municipalities.

In the reputation of those organizations such as hospitals, not-for-profit hospitals, Nassau County Medical Center, and other municipality facilities, they don't want to simply institute litigation against an individual who is financially unable to pay.

Senator D'AMATO. You are really a lawyer. It took a long time to answer a question. You could have said yes. [Laughter.]

You follow a policy to ascertain whether there are some assets prior to our commencing suit; right?

Mr. LANDAU. Correct. [Laughter.]

Senator D'AMATO. Terrific.

Mr. LANDAU. As far as the judgments that are presently on hand, as Mr. Dawson indicated, we would have to take a review before an intelligent response could be given. But, based upon our experience that 75 percent of the dollars collected are collected after we institute legal action. So we include legal action against $1 million, we will collect approximately $750,000 of that $1 million.

Senator D'AMATO. Do you find that to be the case in the area of the defaulted student loans?

Mr. LANDAU. On those that we sue, correct.

Senator D'AMATO. OK, of those that you institute?

Mr. LANDAU. That is correct.

Senator D'AMATO. So, we establish it. You make the determination you don't sue everyone that walks and moves. That is important because the Federal Government doesn't want you out there suing the whole world.

I am sure the Attorney General has an interest in this, too. It is those kinds of things that are important to understand clearly for the record.

Mr. Dawson?

Mr. DAWSON. Yes, sir, the next step within the judgments or litigation steps is the psychology aspect. As Dick Hastings of the Department of Education has so kindly reiterated, the fact that when a collector telephones debtors, he doesn't have the ability to threaten any

action. His hands are, therefore, somewhat tied other than simply asking the individuals to pay, and trying to get them to cooperate with us.

Senator D'AMATO. So yours has been a rather frustrating experience, to say the least?

Mr. DAWSON. Yes, sir, and we appreciate the support that Dick Hastings has given as well as the support of the entire Department of Education.

They have been extremely supportive of the problems that we run into in this area.

Senator D'AMATO. You cannot even say that unless you make the payment that a lawsuit can be instituted against you, can you?

Mr. DAWSON. No, sir.

Senator D'AMATO. That word kind of spreads quickly throughout the community. They know that.

Mr. DAWSON. That is correct. That is the psychology of it. Once litigation can be enforced through third parties and such action is being taken, we strongly recommend that the public be informed of this fact as the Attorney General has done through the U.S. Attorney's Office in Philadelphia when they repossess cars and take various steps around the country. That is the psychological step.

Mr. BURKE. Senator, I am Ed Burke. The Fair Debt Collection Practices Act which Mr. Hastings referred to has a provision in it that states if a debtor writes a collection agency and demands no more contact, the agency cannot contact that individual again except for telling him what steps will be taken.

When this happens to our clients in the private sector, G C Services writes the individuals stating that they will not be contacted, but the accounts are going to a lawyer immediately. The letters are reasonably effective. We cannot do this with Federal Government accounts because authority does not exist for the private sector to file suit on these accounts. We are rather hamstrung. People are taking advantage of the law.

Senator D'AMATO. It is almost all you can do to identify people, track them down, prepare the cases for litigation, but then there has to be that followup, someone who is going to sue. Otherwise there are a lot of hours, work, time and effort, and all it leads people to believe quite correctly is that, listen, I don't have to pay. There is nothing they are going to do to me.

Mr. BURKE. The attitude is that this legislation was created by the Federal Government to make the borrowers immune from Federal loans.

Senator D'AMATO. Let me commend you for undertaking the work that you have without the necessary tools though. It is, obviously, rather frustrating. It has not paid the kind of dividends that I think it can and should. We have to work to see that it does. Again, what I am concerned about is the growing tendency on the part of some to attack the underlying loan programs because of growing defaults.

I feel very strongly that we have an absolute commitment and obligation to maintain guaranteed student loan programs. It is so important if we are going to compete as a Nation in the future, to give educational opportunity, students have a right to expect assistance, but they also have a responsibility to pay back the loans.

So whether it is a guaranteed loan program, the Small Business Administration programs, others, they come under increasing attack. It is a scarce tactic. The citizenry becomes outraged over it, they become upset about the size of the loan defaults.

The very programs themselves that most people think are important become subject to the attack. So I think what Senator Percy is attempting to do is to say, let's go after these delinquencies, let's see to it that, number one, Americans pay back and these loans should be paid back.

In this way we can keep those programs and correct the abuses that exist within them.

So I feel rather strongly about it.

I thank you for coming in, for your testimony.

I thank Mr. Landau, for the many, many hours that you have spent here in Washington working with the Education Department and conferring with the Justice Department.

I think your willingness to come forward—granted that you seek greater participation for your firm—is to be commended. Irrespective of which law firms are engaged, I think the process that we suggest makes eminently good sense.

This is a rather marked turnaround, in savings we think outside law firms should be retained for the litigation of Government debt cases.

Now there is the question of how we get to the point of implementing that. That is what I am concerned about. I don't want a statute on the books which is not effective.

So I think we have made great progress.

Mr. Dawson, I want to thank you and your associates for coming in.

Mr. Landau, it is good to see you again and I thank you for the time that you have given to this committee and to this important national effort.

[The prepared statements of Messrs. Landau and Dawson follow:]

STATEMENT

OF

BERNARD D. LANDAU
SENIOR & MANAGING PARTNER
OF HAYT, HAYT & LANDAU

Before I give my testimony at this hearing, I would like to introduce three of my partners who are directly involved with the various collection programs of our law firm; Robert S. LeWinter, Richard A. Nicoll, and Alan D. Reffkin, who is the resident partner of our Washington, D.C. office.

I consider it a privilege and an honor to have been asked to appear before this distinguished Subcommittee which is seeking information as to whether or not the commencement of litigation by private sector attorneys is feasible and/or necessary to the effective collection of delinquent debts owing to the United States Government.

I would like to offer some brief background information relating to my firm and myself as an introduction to the comments which I will be presenting today.

I have been practicing law in the State of New York for 27 years, and today I am the Senior and Managing Partner of the national law firm of Hayt, Hayt & Landau. We presently employ over 750 people including 85 attorneys, 34 of whom are partners. We have 16 offices in 11 states (Great Neck, New York; New York City, New York; White Plains, New York; Phoenix, Arizona; Los Angeles (Woodland Hills), California; Miami, Florida; Orlando,

Florida; Atlanta, Georgia; Chicago (Evanston), Illinois; Boston (Lynnfield), Massachusetts; Rockville, Maryland; Tinton Falls, New Jersey; Albuquerque, New Mexico; Philadelphia, Pennsylvania; Washington, D.C.; and London, England). The firm, (Hayt & Hayt), was founded in 1929, and when I joined it in 1955 there were three partners and five employees. In the 26 years that I have been a partner, I have directed its growth to its present national stature. While we conduct a large general practice, we enjoy a national reputation of being the largest law firm in the United States specializing in collection. In 1966, we started to develop our own data processing systems and currently maintain over 400,000 active collection files - 95% of which are consumer debts.

Although the firm has been involved with collection work for more than fifty years, we have witnessed a tremendous increase in referrals from every type of industry which we represent. As an example, in the past ten years we have received approximately 2.5 million accounts with a total dollar value of approximately 1.2 billion dollars. In the prior 44 years, we received probably one-tenth of these amounts. In 1982 alone, on a national basis, our firm received 365,471 accounts with a total dollar value of $355,743,865 and collected approximately 85.2 million dollars. This represents a liquidation rate of 23.9%. Our total inventory is turned over in an average of two years and our ultimate liquidation on consumer claims is about 38%.

The proliferation of credit cards and easy credit terms have transformed the American consumer public into a credit society. Not only is it desirable, but in many instances, necessary for an American consumer to obtain some form of credit.

During the past ten years, our law firm has performed collection services for various municipalities and governmental agencies. During this time we have been able to assess the differences in attitudes of the various consumer debtors. The most striking factor which sets collection of debts owed to the government apart from collection of debts in the private sector is the unwillingness of the debtor to repay the government. While in the private sector, those who borrow realize that they have a legal obligation to make repayment, it would appear that many Americans view government loan programs as an entitlement rather than an obligation that must be repaid. Regardless of whether the debt stems from hospital services, the imposition of a fine, or some form of loan, it is apparent that the attitude of many debtors is that the services or obligation do not have to be paid for, or more significantly, that the government will not or cannot pursue payment. In fact, several contracts which our firm entered into with governmental entities initially excluded litigation. In each instance, as predicted, the initial collection results, although significantly greater than those achieved by the municipality itself, did not produce the type of results which we would

consider satisfactory, had we been authorized to institute legal action. In each instance, we eventually prevailed upon the municipalities in question to permit us to institute legal proceedings. The results were dramatic when compared with the efforts of the Corporation Counsel of the City of New York and other County Attorneys. Although no two programs are the same, our law firm has been able to establish programs to fit the unique needs of the particular municipality or agency.

Where the firm has been given the right to institute suit, collection results improve significantly. Based upon our experience in dealing with governmental debt collection programs, it is our opinion that once the debt collection effort is supported by an immediate and effective legal collection program, results can increase twentyfold. However startling as this statement may appear, it is true and an accepted fact in the collection industry that a collection effort without legal action will produce far fewer dollars.

Recently, attention has been focused on the disappointing results achieved by two national collection agencies in their efforts to collect delinquent student loan accounts on behalf of the United States Department of Education. Following the initial implementation of the collection program, the contractors have

recommended that, in order for the program to be successful, the government must avail itself of outside legal services to pursue litigation. The reason underlying the recommendation is simply that the debtors involved are convinced that the government has neither the inclination nor the capacity to pursue hundreds of thousands of claims through the courts. Consequently, these student debtors believe that their obligations will ultimately be forgotten or barred by the Statute of Limitations. Results to date show this to be correct as millions of dollars are being lost through inaction.

In July of 1981, the Department of Education prepared a request for proposal (RFP 81093) dealing with the collection of delinquent student loans. The RFP consisted of three contracts, each national in scope, providing for the work to be performed out of Atlanta, Chicago, and San Francisco. The three-year contract contemplated placing approximately 864,000 delinquent accounts with a dollar value of more than 1 billion dollars ($1,039,040,000) with private contractors. This RFP specifically solicited collection activity and prohibited the threat of or commencement of legal action by the outside contractors. For over one year now, the delinquent accounts have been placed with the two collection agencies awarded the contract pursuant to the RFP. The results have, regrettably, been significantly less than anticipated. The Department of Education now recognizes what the

collection industry and the collection bar have known for years; that effective collection must, as a necessary element, include litigation. Based upon the contemplated placements and our expertise in the area of consumer debt collection, we would conservatively estimate that approximately 35%-40% of all accounts placed for collection by the Department of Education will require legal action. This translates into approximately 350,000 delinquent student loan suits which will have to be commenced in the immediate future to prevent these actions from being barred by the Statute of Limitations of the various states.

It is evident from the foregoing that not only is there a serious problem in theory, but a practical problem in resolution. According to the American Bar Association, there are approximately 612,593 practicing attorneys in the United States. However, it is our belief that no more than 5,000 of these attorneys are handling consumer collection accounts on a regular basis. Accordingly, only .8% of all available attorneys in the private sector possess the knowledge and ability to pursue the delinquent debts of the Department of Education. A recent report by the General Accounting Office (Report No. GAC-AFMD-813-57) reveals that at the end of fiscal year 1982, total government receivables increased to approximately 200 billion dollars, of which the sum of 38 billion was delinquent. Additionally, 14 billion dollars of this figure consists of non-tax delinquencies. The report also states that from 1980 to 1982 the delinquent amount due the federal government

increased by 37%. The recovery of these delinquent debts ultimately falls within the province of the Department of Justice.

While there may be 5,000 attorneys in the private sector specializing in consumer collections in the United States, there are only 1,997 Assistant United States Attorneys in the entire country. Furthermore, in all of 1981, fewer than 31,000 suits of any nature were commenced in which the U.S. government was the party plaintiff. This figure represents both criminal and civil prosecution of all statutes enforced by the federal government, and, in total, is less than one-tenth of the anticipated number of suits which must be commenced on behalf of the Department of Education if effective collection is to be realized. It should be further noted that the federal court system currently suffers from overloaded calendars, and in my opinion, could not possibly handle the volume of law suits that would have to be instituted in the next ten years. Attorneys in the private sector will utilize the state court systems which will expedite the total legal process.

None of the foregoing should be construed as an attack on the professional competence of the U.S. Department of Justice or its attorneys. I feel that their competence is well documented and need not be examined. However, when the issue is one of handling hundreds of thousands of law suits, the Justice Department simply is not equipped to take on the job. The major portion of the work must be performed by attorneys in the private sector.

The problem facing the government is not going to be resolved by playing a numbers game - concerning how many dollars are presently in default - how many individual debtors there are - how many attorneys are presently employed by the U.S. Department of Justice, or how many attorneys there are in the private sector. The only way the present problem is going to be addressed and resolved is by the utilization of computers and the employment of attorneys in the private sector who have been handling consumer debt collection for many years.

Last year, my firm alone instituted approximately 30,000 law suits, to bring about a collection result of more than 85 million dollars. While many dollars were collected without ever serving a summons and complaint, the important factor is that when we made a determination that legal action was necessary on a particular account, the summons and complaint was issued in a matter of days. While we instituted 30,000 law suits in 1982, had it been necessary we could have instituted 100,000! Our ability to handle such a large volume had its genesis in 1966, when we started to develop our own computer system. It took us two years to complete the necessary programming and systems work and, by September 1, 1968, we converted 20,000 manual files to a computerized system. Over the past thirteen years, our system has been dramatically upgraded and, by mid-1984, we will be on-line. Our system has the capability of receiving accounts computer to computer, rather than

through the traditional manual method of writing up files. When legal action must be instituted, our legal staff reviews the file and a request is put into the computer to produce a summons and complaint. Three times a week, the computer reviews every file on the system, and if a summons and complaint has been requested, the computer produces the necessary legal documents. Our computer system can produce approximately 23,000 legal documents in a 24-hour period. Although the summons and complaint initiates the law suit, there are numerous other factors that enter into the total process. These factors include monitoring process servers, the entry of default judgments, preparing income executions, restraining orders, satisfactions of judgment, and most important of all, the reporting of status to our clients on every account on a monthly basis.

Although the "Debt Collection Act of 1982" was a necessary and valuable piece of legislation, it has not stemmed the tide of delinquent consumer debts owed to the government which continues to increase. In fact, only a few federal agencies over the past several years have formulated collection programs for the recoupment of federal loans or guaranteed obligations, and even if these agencies were to forward accounts to private collection agencies for additional collection effort, without an effective legal collection program, all credibility with regard to repayment of the obligation will have been destroyed. However, once the

community of debtors realizes that a demand for payment will be followed by immediate legal action, overall collections will increase dramatically. The federal agencies themselves will realize greater collections, the collection agencies contracting with various federal agencies will see increased collections, and the legal process itself will bring in untold millions of dollars. It has been our experience that once an effective legal program is put into effect for a municipality or governmental agency, the general public realizes that they are of serious intent and they will start paying their bills in the same manner as they recognize their obligations to private creditors.

As an example of the necessity for the commencement of litigation for an effective collection program, let me offer the following statistics. In 1982, our New York office received 191,510 accounts with a dollar value of $196,589,625. During the same year, we were able to effectuate collections in the amount of $58,849,193 resulting in a liquidation of 30.0%. In the area of student loans, our firm collected in excess of one million dollars, the substantial portion of which was realized after legal action was instituted. In 1983 we expect to collect in excess of 5 million dollars on our student loan portfolio.

For the past five years, the law firm has developed expertise in the collection and litigation of delinquent student loan accounts. We perform these services for state guarantee agencies as well as for individual institutions (i.e., New Jersey Higher Education Assistance Authority; Massachusetts Higher Education Assistance Corporation; Pennsylvania Higher Education Assistance Agency; Rhode Island Higher Education Assistance Authority; Connecticut Student Loan Foundation; Long Island University; Hofstra University; Bucknell University; Chicago Medical School; Indiana University; Northwestern University and Princeton University). In our efforts to collect student loans, we have seen all too clearly the need for litigation in order to resolve the account successfully. Let me offer some specific examples that speak to this fact:

Situation 1

We received a delinquent student loan account where the debtor was employed by a state Governor's Office of Employee Relations. The debtor refused to make payment and legal action was commenced and reduced to judgment. Once post-judgment remedies were commenced, the debtor remitted $4,282.62 to pay his account in full.

Situation 2

A law clerk for a State Supreme Court Justice refused to pay his student loan. Legal action was commenced and reduced to judgment. Pursuant to state law, a restraint was placed on the defendant's bank account, depriving him of access to his funds. Shortly thereafter, we received a check for $1,500 which paid the account in full.

Situation 3

We received a delinquent guaranteed student loan in the amount of $20,000. The debtor was an orthopedic surgeon. The doctor offered $200 per month to resolve the account. Legal action was commenced, a judgment obtained, and a levy issued to the Sheriff. The debtor and his family raised $20,000 to pay the account in full.

Situation 4

An artist had an outstanding loan in the amount of $3,500. Originally, he offered a piece of sculpture in settlement of his debt. He later increased his offer to a payout of $40 per month. After both offers were rejected, legal action was commenced. Within two weeks of being served with legal process, he forwarded his check for $3,500 to pay the account in full.

Situation 5

An assistant county attorney was delinquent on a $10,000 student loan. A stipulation of judgment and payout were agreed to. Thereafter, the debtor breached his agreement and his bank account was attached and all his funds withdrawn. The debtor has since regularly made each monthly payment.

Situation 6

An advertising executive for a national radio station stated that she had no intention of paying her delinquent student loan because none of her friends were paying their loans. After we obtained a judgment, and garnished her wages, she borrowed the amount of the judgment ($3,750) and paid the account in full.

The foregoing represent but isolated incidents of individuals who did not believe it necessary to repay their student loans and did so only after the commencement of litigation. The effectiveness of a legal program is not limited to student loans alone, but runs the gamut of all consumer and commercial debts. As a result of "consumerism", debt collection laws and regulations, and sophistication of debtors, creditors now find themselves in a defensive posture. We maintain that only by utilizing the legal remedies available do creditors gain a fair chance of recovering monies owed to them.

We recommend that appropriate legislation be enacted which will allow the private sector of attorneys to assist and supplement the collection efforts of the various federal agencies as well as the Department of Justice. As previously stated, the major element to consider is the magnitude of the current problem. While many attorneys can reduce claims to judgment, it takes truly unique talents to be effective in producing collections on judgments. It would appear that the Department of Justice has neither the manpower nor the computerized systems to deal effectively with the problem on a large-scale basis. To deal with the problem, it will be mandatory to computerize fully any collection effort on the part of the Department of Justice for effective handling of the anticipated volume over the coming years. Regardless of what resources are made available to the Department of Justice to accomplish this, it will take several years. Accounts must be transferred computer to computer. To do the job effectively, the private sector of attorneys will also have to have computer capabilities to allow maintenance and control of files, commencement and conclusion of legal actions, and the ability to report status and statistical data. Once legal action is commenced in the various state courts and a judgment secured, the government would benefit by the award of interest and statutory cost, pursuant to the various state laws. These additional funds, over and above the principal and interest due at the time of placement would significantly defray the contingency

rate which will have to be paid to the private sector attorneys. It is conceivable that a successful legal program by the private sector would be at marginal cost to the government. The alternative would be significant and massive staffing of the particular governmental agency with in-house attorneys, if the law permits, or increasing the staff of the Department of Justice. In my opinion, the cost would not justify the result. The average claim in the student loan program is $1,200. In fiscal year 1982, the Department of Justice claims that they collected $200,132,541.How much of this money was collected from individual delinquent debtors rather than corporations we do not know nor we do know the value of the average claim handled by the Department of Justice during this period. It is our belief that the average claim was far in excess of $1,200. There is no question that collection cost per dollar collected is reduced dramatically when the average claim is increased. While the Department of Justice claims that their average cost per dollar collected is 6¢, based upon our experience I doubt that this figure is applicable to their student loan portfolio. Presently the Department of Justice purports to bring actions only on claims for $600. or more. It is our opinion that with a good home address and positive asset information, such as a place of employment or bank account, legal action is justified on claims of $300 or more, provided the paper work and monitoring of the legal process is done by lawyers and paralegal staff in conjunction with computers.

Insofar as each state has a Statute of Limitations during which legal action must be commenced in order to be timely, the federal government is at a crossroads in their debt collection effort. For each day of delay in establishing an effective legal collection program, claims will be time barred and lost forever. In times of governmental cutbacks, it is imperative that the government reduce its bad debt and thus replenish funds for current programs from existing debtors.

In 1976, our law firm commenced a legal program on behalf of a major municipal agency and commenced approximately 50,000 law suits in one year. We believe this litigation record by a single law firm has never been matched in the history of American jurisprudence. We are currently suing approximately 30,000 people each year. Since we have a comprehensive legal computerized system in place, we estimate that within the next twelve months we could initiate, on a national basis, at least 150,000 law suits which could significantly impact on those federal bad debts requiring litigation.

The foremost and most obvious requirement prior to the commencement of legal action is that the creditor must know the correct home address or place of employment of the debtor. Given the mobility of American society today, this is no small task. However, as a result of the access that many governmental agencies

have to Internal Revenue Service records, we believe that the major stumbing block in an effective legal program can be overcome. Through the electronic transmittal of accounts to the private sector attorneys, and the ability to make massive and rapid inquiry to the IRS data base, we believe a legal program could be effectuated within a relatively short period of time. The creation of such a program, coupled with the vast resources of the government itself will ultimately establish the credibility currently lacking in the government debt collection efforts.

In conclusion, it has been my objective to make this Subcommittee aware of the importance of legal action in resolving the debt collection problem of the United States Government. The present situation is depriving the government of an enormous sum of money, which is needed to facilitate the continuance of their various programs. The government is faced with the immediate need for outside legal services, possessing the specialized skill of private sector collection attorneys.

Mr. Chairman, I thank you for the opportunity to appear here today, and sincerely hope that you find my comments helpful in your future deliberations. And now, Mr. Chairman, I would be pleased to respond to any questions you or other members of the Subcommittee may have.

PREPARED STATEMENT OF G. L. DAWSON

Mr. Chairman and gentlemen, my name is Bob Dawson and I am Vice President of G C Services Corporation.

G C Services is based in Houston, Texas and has 38 field collection offices and 24 marketing offices nationwide. Today, we employ over 1800 individuals and thus are the largest third party debt collection organization in the United States. We are currently servicing more than six million new accounts every year, including the largest contract awarded by the Department of Education to the private sector. In addition, G C Services is currently operating the pilot program to create an in-house automated collection system for the Internal Revenue Service. This program is presently operating in the IRS offices in Chicago, St. Louis and Kansas City.

We thank Chairman Percy and the Subcommittee for the opportunity to present our views on the collection of debts owed to the Federal Government. We wish to address two areas in particular: (first) the urgent need for private sector litigation authority to collect federal debts, and (second) the status of our efforts to work with various government agencies.

Before addressing these concerns, I would like to express our gratitude and full support of the commitment this Administration has made to recover debts owed to the U.S. Government. We are especially pleased with efforts by the

Office of Management and Budget to improve debt collection, and with the recent passage of S. 376 which would enable private collection agencies to be compensated on a contingency basis. Both of these initiatives will greatly facilitate government use of expert private collectors in the massive task of recuperating delinquencies.

These measures could have an even greater impact on the collection of federal debts if at the same time, where permissible private sector agencies could acquire the authority to litigate on behalf of the Federal Government. Without that authority, collection agencies have substantially less leverage for collecting Federal debt than for collecting private sector debts.

As of October 1, 1982, the Department of Education had referred 268,259 delinquent accounts to G C Services for collection. These accounts amount to $364,830,871. Each account represents a defaulted student loan under the National Direct Student Loan (NDSL) Program or the Federally Insured Student Loan (FISL) Program. At present, approximately 25% or 67,000 of these student debtors have been located. Of those located, about 15% or 8,000 cases will require litigation for collection. G C Services projects that a minimum of 15% of all delinquent accounts will require litigation. Such litigation would represent a minimum potential collection of nearly $55

million based on the number of accounts presently assigned to G C Services.

In handling these accounts, our experience shows that without our ability to litigate, many debtors deliberately fail to pay their debts. Thousands of debtors have told us they are aware that no legal action will be taken against them for refusal to pay, and therefore they do not.

At present their assumption is correct. The Department of Justice simply does not have the necessary resources to initiate such a massive litigation program.

The Justice Department has acknowledged that cases totaling close to $1 billion await litigation. The actual dollar amount is significantly higher since the Department may not be including in its estimate the large number of cases involving less than $600. In addition, there are many other cases which have not yet been processed at Justice because a computerized system to handle referred accounts coming from various agencies is not in place at the Justice Department.

Even if the Department of Justice were to complete court action in each case, there is no mechanism in place for enforcing judgments. At present, no specific department exists within Justice for judgment control and enforcement. In fact, enforcement is not even considered a legitimate workload item. Consequently, there are no incentives to follow through on

judgments. The little that has been done in the Justice Department has been mainly clerical work.

In some instances, the Justice Department has referred judgments to the agency pursuing collection. We feel this procedure is unsound because without the authority to litigate, an individual agency is not likely to have staff appropriately trained for such enforcement. Nor is enforcement of Justice's judgments properly within the jurisdiction of another agency. Requiring separate agencies to enforce judgments is not consistent with current policy precluding agency input on judgment amounts. In this regard, there have been cases where the Justice Department has settled for a lesser amount than reasonably expected by the agency involved.

Conceptually, we believe that the contract between the Department of Education and G C Services Corporation was rooted in the philosophy that there are certain functions previously performed by Governmental Agencies that may be performed more efficiently and less expensively by the private sector. We believe that this concept has great merit and will prove to be highly beneficial to the government when pursued in a complete manner.

It is our judgment that under the present circumstances delinquencies are not and can not be pursued in a manner comparable to those in the private sector.

The collection of delinquent loans from students involves not only the mechanics of collection but the psychology of repayment incentives as well. Our collection effort on an individual debtor is not operating in an isolated environment. Delinquent debtors are in a fairly circumscribed age group. Most of them know other individuals who similarly had student loans. We are dealing with individuals who have a sophisticated awareness that tens of thousands have not repaid their student loans; and that despite their delinquency, virtually no disciplinary action has been taken against them. Consequently, their refusal to repay their loans is a normal behavioral reaction, absent any incentives to the contrary. It is therefore critical that we institute some system of incentives to alter that behavior.

It is our judgment that an effective program of legal process through the use of local private attorneys could serve as the framework for such a system of incentives. It could do so on the basis of improving collection through the actual legal process, and of substantially enhancing the psychological environment for repayment.

To handle such a program effectively requires an established network relationship with thousands of attorneys throughout the United States. Many jurisdictions require that an individual be sued in his local community or county. G C

Services has such a network of attorneys familiar with local and regional court requirements.

Therefore, we respectfully propose that private sector firms be authorized to litigate or to refer selected accounts to private attorneys with whom we have already established long and satisfactory working relationships. It is our opinion that with the proper machinery already in place, judgments could quickly be rendered on a substantial number of accounts.

Further, we recommend that at such time as judgments are satisfied, the appropriate Agency rapidly distribute among the general public the knowledge that the Federal Government is using every facet available by law to collect on delinquent accounts. Such a procedure would begin to build an aura of credibility for our debt collection process.

In addition to the Department of Education, G C Services has had contact with numerous other federal agencies regarding the collection of outstanding debts.

While there is evidence of an increasing inclination to use private sector agencies for the purpose of collecting delinquencies, G C Services believes that the manner in which contracts are being awarded is not necessarily in the manner envisioned by this Subcommittee as it painstakingly drafted the Debt Collection Act of 1982.

For example, the Department of the Air Force recently awarded a contract for collecting debts owed to the Air Force by former employees whose current addresses are unknown. The contract was awarded to two collection agencies for fees of 14¢ and 18¢ on every dollar collected.

Contracts of this type with private sector creditors normally involve compensation at 40¢ - 50¢ on every dollar collected. This high rate is due to the difficulty and high costs associated with locating individuals and convincing them to recompense a former employer. The discrepancy between the average rate and the bids of the two agencies handling the Air Force accounts leaves room for speculation that the two agencies may not use all possible follow through methods for every account. The danger here is that the Air Force would be displeased with the results and determine that use of private sector agencies has not been effective in the collection of federal debts.

To resolve this type of dilemma, G C Services recommends that minimum requirements for work activity be incorporated by the federal agencies into their requests for proposal. The Department of Education used this procedure for the Student Loan program and G C Services supports having other agencies follow this example.

It is sensible in any contract negotiation or bid to specify the acceptable performance standards for a product or

service. Without such standards, the performance of the product or service may not meet the expected or desired level.

The Bureau of Land Management at the Department of the Interior has similarly requested proposals from private collectors to locate former employees and collect debts owed to Interior. As stated earlier, the difficulty in locating these individuals and the costs of following through on efforts to collect result in at least a 40% contingency rate.

In the case of Interior, Public Law 97-394, the FY '83 Interior Appropriations Act, authorizes the Department to use only up to 20 percent from the recovery of the delinquent debt owed to the Government to pay for contracts to collect these debts.

G C Services submitted a proposal to collect the outstanding debts of former employees on May 19, 1983. While we are confident that the technical portion of this proposal is superior, our bid was set at 40% despite the 20% cap. G C Services is a results-oriented organization committed to carrying out the best possible means for collecting delinquent debts. It is unrealistic for G C Services to bid any lower on that type of contract and maintain its reputation for thoroughness. Instead we are hopeful that the 20% cap can be changed since it only sufficiently covers certain contracts such as collection from corporations with known addresses and assets.

Senator D'AMATO. The subcommittee stands in recess.

[Whereupon, at 1:20 p.m., the subcommittee recessed, to reconvene at the call of the Chair.]

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

STATEMENT OF
H. GRANT LAPPIN, JR.
PRESIDENT
OF
ACCOUNTS MANAGEMENT CORPORATION
ON THE
FEDERAL DEBT COLLECTION PROJECT
BEFORE THE
ENERGY, NUCLEAR PROLIFERATION
AND GOVERNMENT PROCESSES SUBCOMMITTEE
GOVERNMENTAL AFFAIRS COMMITTEE
UNITED STATES SENATE

Mr. Chairman, Members of the Subcommittee:

I am H. Grant Lappin, Jr., President of Accounts Management Corporation. Accounts Management Corporation, as one of the ten largest private debt collection firms in the United States, operates nationally through eleven offices and has more than three hundred employees. We wish to commend the Chairman for spearheading the Federal debt collection effort. Although the Federal private debt collection program has now begun, the continued vigilance of this subcommittee is essential to ensure the success of that program.

In the seven months since the enactment of the Federal Debt Collection Act, we have contacted almost thirty Federal departments and agencies with well over ninety percent of the outstanding Federal accounts receivable. While many Federal officials continue to believe that their accounts receivable are unique and, thus, are not amenable to private collection contracting, we are convinced that a debt owed to

the Federal Government does not differ significantly from a debt owed in the private sector. Therefore, even though Federal private collection efforts are still in the preliminary stages, we have nevertheless formulated general recommendations for private contracting based on the efforts to date.

A universal recommendation for Federal private debt collection contracting is to ensure that any Federal solicitation reflects as closely as possible current debt collection industry practice. Because debt collection services are specifically designed in each case by a private firm in accordance with the needs of the creditor, whether commercial or governmental, private debt collection services should invariably be solicited through the use of a request for proposal (RFP), rather than an invitation for bids (IFB). An RFP provides the flexibility for both the Federal Government and those proposers within the competitive range to negotiate the package of services most advantageous to the Government. Conversely, an IFB, which permits competition solely on the basis of price, is designed for the acquisition by the Government of a standardized service or commodity (such as office furniture), and not of a relatively complex and specialized service such as debt collection.

The work that the contractor will be required to perform should be expressly stated in the RFP. Otherwise, private firms may bid a low contingent fee percentage with the intention solely to "skim the cream," that is, engage in efforts to collect only the largest, most collectible accounts. Detailed statements of the work to be performed would also permit the agency to conduct a more thorough pre-award survey of the responsibility of the proposers within the competitive range.

The number of accounts subject to a particular RFP should also be maintained at a manageable level. No single debt collection firm in the United States is large enough to assimilate and to initiate collection efforts simultaneously on hundreds of thousands of accounts. Thus, the accounts receivable for a very large program should be divided into a manageable number for each individual RFP through a regional or other logical categorization.

Moreover, to permit private contractors to initiate collection efforts as rapidly as possible, the prime contractor selected by the Government pursuant to an RFP should be permitted to execute subcontracts with smaller local collection agencies. Thus, Federal departments and agencies should adopt procedures for compliance with the Privacy Act

and any other overriding Federal legislation that are sufficiently flexible to permit subcontracting.

The Federal Government should also adopt RFP procedures that permit the prospective contractor to submit the lowest possible bid that will nevertheless provide an incentive to collect the least attractive accounts. In accordance with standard industry operating procedures, a debt collection agency should be able to propose a graduated or sliding scale contingent fee schedule. The fee percentage would be the highest for the smallest and oldest accounts, and the lowest for the largest and most current accounts. If an agency is permitted to submit only a composite bid with a single contingent percentage for every account, the agency will have little incentive to attempt to collect an older, small account because the monies expended in collection efforts are likely to exceed the amount of the contingent fee for that account.

The contractor should also be permitted to review on-site the work to be performed upon execution of appropriate confidentiality statements. Based upon a brief, but careful, examination of the work to be performed, a private contractor can determine very closely the amount that can be collected, thus enabling the contractor to submit the lowest possible bid.

A private debt collection agency will never be able to collect all of the outstanding account receivables subject by an RFP. Where the debtor remains locatable and solvent, but unwilling to pay, litigation will often be necessary in order to complete the Federal collection process. Because the private debt collection effort will result in the referral to the Department of Justice for litigation hundreds of thousands, and possibly millions, of uncollected accounts, the debt collection backlogs currently afflicting Federal departments and agencies will simply be transferred to the Justice Department. Obviously, Justice will not be able to litigate all of these claims simultaneously.

If a debtor is assured that litigation of the Federal claim will not occur for many years, if at all, the debtor will be much more reluctant to pay its Federal debt notwithstanding the efforts of a private debt collection agency. To avoid this result and to expedite collection, we urge the Subcommittee to promote Federal initiatives to permit private collection agencies to complete the debt collection process by retaining private law firms for litigation of claims not collected by the collection agency. Upon reducing a claim to judgment (which will often be a default judgment since empirically a relatively small percentage of debtors responds to a complaint), the collection agency could then

reinitiate efforts to collect the judgment or refer it again to private attorneys for execution, including garnishment of wages.

The suggestions that I have briefly presented to the Subcommittee are intended to improve the prospects for success of the Federal private debt collection efforts. In order to implement these suggestions, we urge the Congress to provide Federal departments and agencies with adequate resources to assemble and organize accounts and to prepare RFP's for private debt collection contracting. Moreover, resources should be made available in appropriate circumstances for contracts with private collection agencies for consulting services, including the automation of accounts so that they are most expeditiously assimilated and collected by a private collector after the award of a contract.

I wish again to commend this Subcommittee for its efforts to ensure that amounts owed to the United States, and derivatively to all of the citizens of our nation, are collected in the same fashion as a debt owed to a commercial or other private sector creditor. We believe that these efforts will contribute significantly to the fiscal integrity of our Government.

HARVARD UNIVERSITY
1350 MASSACHUSETTS AVENUE
CAMBRIDGE, MASSACHUSETTS 02138

FINANCIAL SYSTEMS

557 HOLYOKE CENTER

May 23, 1983

Mr. Alan Mertz
C/O Senator Charles Percy
Room S.D. 462
United States Senate
Washington, D.C. 20510

Dear Mr. Mertz:

During a recent telephone conversation with Mr. John Maloney, you requested some documentation outlining the steps taken by Harvard University to improve the H.P.S.L. delinquency rate. The following is a list of procedures outlined in our action plan as required by the Department of Health and Human Services:

- All files for delinquent borrowers be reviewed to insure that all documentation has been received and properly implemented.

- That any borrower with missing documentation (i.e. internship and/or residency deferment) will be contacted and given an opportunity to replace the documents.

- Borrowers be contacted and asked to pay the outstanding payments for any period not covered by certified deferment documentation.

- Borrowers unable to pay overdue amount and/or increase their monthly payments, must continue with their regular repayment schedule while documenting their financial difficulties.

- Borrowers unwilling to meet the prescribed repayment schedule after the efforts of the collection department over a 120 day period - have their loans assigned to an attorney or collection agency for disposition.

- That all borrowers presently at an attorney or collection agency be reviewed and any inactive (no payments for 6 months and assigned for a 2 year period) be prepared for submission to HHS for consideration or a write-off.

Please let me know if I can be of further assistance.

Sincerely,

Paul F. Leary
Associate Director
Financial Operations

PFL:jn

O.M.B. No. 51-R0147

NAME AND ADDRESS OF SCHOOL	PERIOD COVERED BY THIS REPORT	SCHOOL ED. NUMBER
Harvard University College of Medicine, 25 Shattuck St., Boston, MA 02115	July 1, 19 79 through June 30, 19 80	O 1 L 250058-80 B H L 10

SECTION III

1. STUDENT LOAN PROGRAM

[X] FEDERAL CAPITAL CONTRIBUTION FUND [ ] FEDERAL CAPITAL LOAN (NDSL) FUND

2. FINANCIAL REPORT	CUMULATIVE FROM BEGINNING (LOANS ONLY)	CURRENT FISCAL YEAR
A. FEDERAL FUNDS AUTHORIZED	$ 2,979,612.81	$ 54,583.00
B. CASH BALANCE BEGINNING THIS FISCAL YEAR		72,039.15
C. CASH RECEIPTS		
1. FEDERAL FUNDS RECEIVED/RECEIVABLE	2,979,612.81	54,583.00
2. INSTITUTIONAL CONTRIBUTIONS DEPOSITED	319,134.49	17,396.23
3. TRANSFER FROM SCHOLARSHIP FUND (FCC ONLY)	-	-
4. LOAN PRINCIPAL COLLECTED	922,901.39	165,473.89
5. INTEREST INCOME COLLECTED ON LOANS	262,327.84	41,369.85
6. OTHER INCOME (Specify)	-	-
7. TOTAL CASH RECEIPTS (C.1 through C.6)	$ -	$ -
D. CASH AVAILABLE (B. Plus C.7)	$ 4,483,976.53	$ 350,862.11
E. CASH DISBURSEMENTS		
1. LOAN TO STUDENTS	$ 4,272,736.96	$ 349,045.67
2. TRANSFER TO SCHOLARSHIP FUND (FCC ONLY)	209,386.20	-
3. REPAYMENTS TO FEDERAL GOVERNMENT	-	-
4. RECONCILIATION ADJUSTMENTS (DEAFS ONLY)		-
5. REPAYMENTS TO INSTITUTION	-	-
6. COSTS OF LITIGATION	-	-
7. OTHER COSTS (Specify) Collection Cost Agencies	1,853.37	1,816.44
8. TOTAL CASH DISBURSEMENTS (E.1 Through E.7)	4,483,976.53	350,862.11
F. FEDERAL FUNDS NO LONGER AVAILABLE ((A. MINUS C. 1) PLUS E. 4)		0
G. CASH BALANCE END FISCAL PERIOD COVERED BY THIS REPORT (D. MINUS E 8)	$ 0	$ 0

H. LOAN CANCELLATIONS	CUMULATIVE FROM BEGINNING			CURRENT FISCAL YEAR		
	NUMBER OF BORROWERS	PRINCIPAL CANCELLED	INTEREST CANCELLED	NUMBER OF BORROWERS	PRINCIPAL CANCELLED	INTEREST CANCELLED
1. EMPLOYMENT						
a. HP PRACTICE-SHORTAGE (15%)	3	2,115.00	-	-	-	-
b. HP PRACTICE-RURAL SHORTAGE (15%)	4	4,057.00	787.56	2	2,735.18	787.56
c. NURSING EMPLOYMENT (12%)						
d. NURSING EMPLOYMENT (15%)						
e. NURSING EMPLOYMENT (23%)						
2. DEATH OR DISABILITY	10	29,271.70	-	1	1,640.04	-
3. BANKRUPTCY (FCC ONLY)						
4. UNCOLLECTIBLE ACCOUNTS (FCC ONLY)						
TOTAL	17	35,443.70	787.56	3	4,435.22	787.56

I. ACCOUNTS OVERDUE	NO. OF BORROWERS	PRINCIPAL PAST DUE	INTEREST PAST DUE
REPORT AMOUNTS MORE THAN 120 DAYS DELINQUENT AS OF JUNE 30 (required)	209	$ 158,727.17	$ 14,813.60
BANKRUPTCY (FCC ONLY)	-	-	-
TOTAL	209	158,727.17	$ 14,813.60

I certify that this report is true and correct and that all financial transactions reported above have been made in accordance with the terms and conditions set forth in the application to participate in the program.

3A. SIGNATURE OF INSTITUTIONAL OFFICIAL OR STATE AGENCY OFFICIAL	3B. TELEPHONE NUMBER (Area Code and Number)	3C. DATE
Kenneth D. Higgins	(617) 495-3782	9/2/1980
TYPED OR PRINTED NAME AND TITLE OF SIGNATURE	SIGNATURE	

BEST AVAILABLE COPY

• U.S. GOVERNMENT PRINTING OFFICE: 1981 720-119

Form Approved
O.M.B. No. 51S-R001

NAME AND ADDRESS OF SCHOOL	PERIOD COVERED BY THIS REPORT	SCHOOL I.D. NUMBER
Harvard University School of Medicine 25 Shattuck St., Boston, MA. 02115	July 1, 19 80 – through June 30, 19 81	011 250058-80 BHL10

SECTION III

1. STUDENT LOAN PROGRAM

☒ FEDERAL CAPITAL CONTRIBUTION FUND ☐ FEDERAL CAPITAL LOAN (REF) FUND

2. FINANCIAL REPORT	CUMULATIVE FROM BEGINNING (LOANS ONLY)	CURRENT FISCAL YEAR
A. FEDERAL FUNDS AUTHORIZED	$3,076,325.81	$96,718.00
B. CASH BALANCE BEGINNING THIS FISCAL YEAR		0
C. CASH RECEIPTS		
1. FEDERAL FUNDS RECEIVED/RECEIVABLE	3,076,325.81	96,713.00
2. INSTITUTIONAL CONTRIBUTIONS DEPOSITED	318,548.92	(585.57)
3. TRANSFER FROM SCHOLARSHIP FUND (FCC ONLY)		
4. LOAN PRINCIPAL COLLECTED	1,106,197.55	183,296.16
5. INTEREST INCOME COLLECTED ON LOANS	312,285.55	49,957.71
6. OTHER INCOME (Specify)		
7. TOTAL CASH RECEIPTS (C.1 through C.6)	$	$
D. CASH AVAILABLE (B. Plus C.7)	$4,813,357.83	$329,381.30
E. CASH DISBURSEMENTS		
1. LOAN TO STUDENTS	$4,539,740.29	$267,003.33
2. TRANSFER TO SCHOLARSHIP FUND (FCC ONLY)	209,386.20	
3. REPAYMENTS TO FEDERAL GOVERNMENT		
4. RECONCILIATION ADJUSTMENTS (DFAPS ONLY)		
5. REPAYMENTS TO INSTITUTION		
6. COSTS OF LITIGATION		
7. OTHER COSTS (Specify) Other Collection Costs	3,106.21	1,252.84
8. TOTAL CASH DISBURSEMENTS (E.1 Through E.7)	4,752,232.70	268,256.17
F. FEDERAL FUNDS NO LONGER AVAILABLE ((A. MINUS C. 1) PLUS E. 4)		0
G. CASH BALANCE END FISCAL PERIOD COVERED BY THIS REPORT (D. MINUS E 8)	$ 61,125.13	$ 61,125.13

H. LOAN CANCELLATIONS	CUMULATIVE FROM BEGINNING			CURRENT FISCAL YEAR		
	NUMBER OF BORROWERS	PRINCIPAL CANCELED	INTEREST CANCELED	NUMBER OF BORROWERS	PRINCIPAL CANCELED	INTEREST CANCELED
1. EMPLOYMENT						
a. HP PRACTICE-SHORTAGE (10%)	3	2,115.00				
b. HP PRACTICE-RURAL SHORTAGE (15%)	4	4,057.00	787.56			
c. NURSING EMPLOYMENT (10%)						
d. NURSING EMPLOYMENT (15%)						
e. NURSING EMPLOYMENT (20%)						
2. DEATH OR DISABILITY	11	30,717.35		1	1,445.65	
3. BANKRUPTCY (FCL ONLY)						
4. UNCOLLECTIBLE ACCOUNTS (FCL ONLY)						
TOTAL	18	36,889.35	787.56	1	1,445.65	

I. ACCOUNTS OVERDUE	NO. OF BORROWERS	PRINCIPAL PAST DUE	INTEREST PAST DUE
REPORT AMOUNTS MORE THAN 120 DAYS DELINQUENT AS OF JUNE 30 (regular)	225	$ 183,955.58	$ 16,009.30
BANKRUPTCY (FCC ONLY)			
TOTAL	225	$ 183,955.58	$ 16,009.30

I certify that this report is true and correct and that all fiscal transactions reported above have been made in accordance with the terms and conditions set forth in the application to participate in the program.

3A. SIGNATURE OF INDIVIDUAL PREPARING THIS FORM	3B. TELEPHONE DATA (Area Code and Number)	3C. DATE
John D. Stone	(617) 495-1889	9/9/81
3D. NAME AND TITLE OF AUTHORIZED FISCAL OFFICER	3E. SIGNATURE	

BEST AVAILABLE COPY